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IN THE

Supreme Court of the United States

OCTOBER TERM, 1953

No. [redacted] 30

THE REPUBLIC OF CHINA,

Respondent,

and

THE SHANGHAI-NANKING RAILWAY ADMINISTRATION, MOH HAN, as Director of the Shanghai-Nanking Railway Administration, SAU CHEN, as Deputy Director of the Shanghai-Nanking Railway Administration,

Defendants,

v.

THE NATIONAL CITY BANK OF NEW YORK,

Petitioner.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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THE NATIONAL CITY BANK OF NEW YORK,

Petitioner.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Petitioner, The National City Bank of New York, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit, entered in the above-entitled case on December 8, 1953, affirming the orders and judgment of the District Court dismissing petitioner's two counterclaims setting forth financial obligations of the respondent, The Republic of China, to petitioner, The National City Bank of New York (hereinafter referred to as "City Bank").

Opinions Below

The opinion of the District Court for the Southern District of New York granting plaintiff's motion to dismiss the counterclaims (R. 35) is reported in 108 F. Supp. 766. The opinion of the District Court denying defendants' motion for reargument and for leave to amend the counterclaims (R. 55) is reported in 14 F. R. D. 186. The opinion of the Court of Appeals (R. 64) is not yet reported.

Jurisdiction

The judgment of the Court of Appeals was entered on December 8, 1953 (R. 64). The jurisdiction of this Court is invoked under 28 U. S. C., Section 1251(1).

Question Presented

The question presented is the extent to which a friendly foreign sovereign, which brings suit in the courts of the United States against an American corporation to recover a debt, is entitled to immunity from the assertion against it by the defendant of counterclaims based on debts owing to the defendant by the sovereign.

The word "counterclaim" as here used is limited in scope to the reduction or cancellation of the claim asserted by the plaintiff, by way of set-off or equitable defense. Counterclaims against sovereigns, when permitted, have always been so limited,[1] as distinguished from counterclaims against private persons, which may support affirmative judgments. The petitioner has not sought a judgment against the sovereign, The Republic of China, enforceable beyond the amount of the sovereign's claim against it, although the sovereign owes the petitioner far more than the amount demanded in the complaint.

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[1] *French Republic* v. *Inland Nav. Co. et al.*, 263 F. 410, 412; *Kingdom of Roumania* v. *Guaranty Trust Co.*, 250 F. 341, 343; 24 R. C. L. 811.

Owing to the manner in which this case came to the Court of Appeals for the Second Circuit, whose judgment this Court is now asked to review, the issues have been reduced to a limited and definite compass. By granting respondent's motion to dismiss the counterclaims in a suit by The Republic of China against the City Bank to collect a debt, the District Court, as affirmed by the Court of Appeals, denied to the petitioner the right to plead financial obligations of the respondent owing to it for the purpose of reducing or cancelling the respondent's recovery (R. 35, 41, 64 *et seq.*, 68).

Although the District Court had denied the motion by petitioner to amend the counterclaims, the Court of Appeals, for the purpose of this appeal, treated the counterclaims as, in fact, amended (R. 67). For all purposes here, the allegations of both parties are to be treated as admitted. Therefore, the only question presented is the legal propriety of permitting The Republic of China, a sovereign, to continue its efforts to enforce a debt (a deposit account) owing to it by the City Bank without regard to its own much larger unpaid obligations to the City Bank, which are not otherwise collectible, since the Bank cannot sue the sovereign.

The Court of Appeals agreed with the District Court in its application of the law to the counterclaims (even assuming them to have been amended) which, in brief, was that The Republic of China, because of its sovereignty, was immune from any reduction by these counterclaims of its expected recovery from the City Bank. It held that a counterclaim, such as these, "is the equivalent of an independent suit against that sovereign brought without its consent" (R. 68). But, in so interpreting the law, the Court of Appeals took occasion to say: "We have no high regard for the idea that, without its consent, a government may not be sued for acts which, if done by a private person, would be actionable wrongs. But we feel we must leave to Congress or the Supreme Court any marked diminution of that hoary doctrine (although, in

the belief of many persons, it is basically immoral)" (R. 68).

The issue which this Court is asked to review is simply whether, in a situation such as set forth in the record, the petitioner, an American bank, shall or shall not be required to pay its debt to the sovereign notwithstanding unpaid debts of the sovereign owing to it, thus increasing its already substantial loss, and, obversely, whether the sovereign government shall or shall not be allowed to repudiate in full its own indebtedness to the defendant, instead of satisfying it in part, out of its recovery in the action.

Petitioner denies that the law properly applicable required the results reached by the courts below. A counterclaim (set-off) against a sovereign is not limited to the narrow definitions laid down by those courts. If any rules of law with respect to sovereign immunity exist as found and applied by the lower courts, they are obsolete and should be so declared by this Court. Moreover, even if the restrictive principles referred to by the lower courts are adhered to, the counterclaims here pleaded are well within recognized exceptions to the doctrine of sovereign immunity.

The question relating to the extent of sovereign immunity and the circumstances under which counterclaims may be pleaded against a sovereign voluntarily suing in our courts, as they arise in this case, may be summarized in the following questions:

1. Does a foreign sovereign voluntarily entering our courts to collect a debt against an American corporation waive its immunity for contract obligations which this sovereign owes to that corporation, to the extent of its expected recovery from that corporation?

2. Should any counterclaim (set-off) based upon the contract obligation of a foreign sovereign, pleaded against it in diminution of or to prevent the recovery by that

sovereign, be considered as an independent suit against the sovereign?

3. Where a foreign sovereign suing in our courts has had business relations over many years with an American Bank, from which it is endeavoring to collect a debt, may contract obligations of the sovereign to the defendant Bank, voluntarily incurred for full value in the course of these dealings by the sovereign, be considered as part of the "subject matter of the suit"?

4. When a foreign sovereign has commenced suit in our courts to recover a debt from an American corporation, and the sovereign owes that American corporation debts in equal or greater amount, may these debts be pleaded as counterclaims (set-offs) notwithstanding that they do not arise out of the "subject matter of the opposing party's claim" as that phrase is defined in Rule 13 of the Federal Rules of Civil Procedure?

Statutes Involved

The pertinent statutory provisions are printed in the Appendix, *infra*, p. 19.

Statement

The pleadings set forth three contracts between the parties: the complaint and the two counterclaims (R. 4-7; 23, 25). The action of The Republic of China is to collect from the City Bank a bank account, which was established in New York by transfer of $200,000 from Shanghai, China, in 1948 (R. 13), the very year in which the petitioner advanced funds in Shanghai, China, to the respondent. These advances in the years 1947 and 1948, larger in amount than the bank account, remain unpaid (R. 25) (*post*, p. 6).

The first counterclaim sets forth the following dealings between the parties: In 1920, the City Bank participated in a $5,000,000 loan to the Pacific Development Company,

which was secured by a Chinese Government Treasury Note in the face amount of $5,500,000. This Note was the direct obligation of The Republic of China, respondent here. The loan was not paid at its maturity and, upon the liquidation of the Pacific Development Company, the Note was, in 1928, purchased for the account of the interested banks and the said obligation payable at one of the member banks of the loaning syndicate has since been held by another of them for the benefit of all. The City Bank has a participating interest in the amount of $317,720.93 with interest thereon, no part of which has been paid. The City Bank's interest in this Note was known to The Republic of China, which recognized its indebtedness thereon to the Bank (R. 23, 24, 46, 47, 52).

The second counterclaim sets forth the following dealings between the parties: Between April 1947 and March 1948, the City Bank, through its Shanghai Branch, purchased Chinese Government 36th Year short-term Treasury Notes (commemorative of the 36th year of the establishment of The Republic) under which The Republic of China, respondent, agreed to pay the face amount of each note within three years, with redemptions every six months. Each was by its terms payable in national currency at the U. S. dollar exchange rate of the Central Bank of China prevailing on the respective days of payment and each was payable at the Central Bank of China or at any of its appointed banks, among which were the Shanghai and other eastern branches of the City Bank. Some of these obligations were paid, but there remains the unpaid amount equal to the sum of $391,033.60 for which The Republic of China is indebted to the City Bank, with interest (R. 25, 26, 46, 53).

Proceedings in District Court

This action was commenced in the United States District Court for the Southern District of New York on the 2nd day of May, 1951. The Bank had received adverse claims to the bank account which the respondent sought

to collect from it and, for its protection, invoked procedures provided by § 51-a of the Civil Practice Act of the State of New York, used where interpleader is not possible because of lack of jurisdiction of the adverse claimant.

Because of the procedures relating to adverse claimants, it was not until July 11, 1952, that the defendant served an amended answer (R. 11). The Republic of China thereupon, on September 15, 1952 (R. 34), made a motion in the District Court pursuant to Rule 12 of the Federal Rules of Civil Procedure to dismiss the counterclaims on the grounds:

> "1. That the Court lacks jurisdiction thereof because plaintiff The Republic of China is a friendly sovereign which has not consented to be sued on the matters therein alleged.
>
> 2. That they fail to state claims against plaintiff The Republic of China upon which relief can be granted."

On December 22, 1952, Hon. Irving R. Kaufman, District Judge for the Southern District of New York, granted the plaintiff's motion to dismiss the counterclaims and in the opinion (R. 38), construing the phrase "subject matter of the suit", held the two counterclaims were not within that term, as defined, and the sovereign had not waived its immunity, citing the cases of *United States* v. *New York Trust Co.*, D. C. S. D. N. Y., 1946, 75 F. Supp. 583, and *Republic of China* v. *American Express Co.*, 2 Cir., 1952, 195 F. 2d 230, 233. The court found no other reason to permit counterclaim or set-off here.

Opinion of the Court of Appeals

On December 8, 1953, Judge Frank, writing for the Court of Appeals for the Second Circuit, in a unanimous decision, affirmed Judge Kaufman's decision and judgment on the authority of *Republic of China* v. *American Express Co.* (*supra*) in which that very court had granted

a counterclaim of interpleader, holding that interpleader for adverse claimants was a proper counterclaim, based upon the subject matter of the suit. In support of his contention that the counterclaims here are equivalent to an independent suit against the sovereign without its consent, the court cited *In re Monongahela Rye Liquors*, 141 F. 2d 864, 869 (C. A. 3).

The Court of Appeals also held *arguendo* that, even if a certain letter by the Acting Legal Adviser of the State Department indicated a "trend" or "shift" in policy tending to restrict sovereign immunity of foreign governments to "governmental" or "public" acts, and to exclude from this protection "private" acts or "commercial activities" this would not cause the Court to reverse the lower court's decision dismissing the counterclaims and that the Court was without power to change these concepts of sovereign immunity, any diminution of which it must leave to Congress or the Supreme Court.

The petitioner had presented in argument that the obligations pleaded in both counterclaims were payable at the petitioner bank and that, therefore, under decided cases and pursuant to § 147 of the Negotiable Instruments Law of the State of New York, should be considered as a direction to make payment to the extent of the bank account sought. In neither case did the court find that the counterclaims were payable at the office of The National City Bank of New York. As to the first, the court held that the obligation was not payable at the petitioner's office and that it was "irrelevant for this purpose that the defendant had a part interest in any proceeds of the note" (R. 69) which, as the record shows, was held by one member of the loaning syndicate, and was payable at another member of this same syndicate in New York (R. 24, 52, 53, 54). The finding as to the second was based on an interpretation of Section 25 of the Federal Reserve Act, 12 U. S. C. §§ 601, 604, relating to the operating of foreign branches by an American bank, and on the cases of *Pan-American Bank & Trust Co.* v. *National City Bank*, 6

F. 2d 762, 767 (C. A. 2), with further reference to *In re Harris*, 27 F. Supp. 480 (S. D. N. Y.), *Bluebird Undergarment Corporation* v. *Gomez*, 139 Misc. 742, 249 N. Y. Supp. 319, *Marlboro Trust Company* v. *Elliott*, 86 F. 2d 315, 316-317.

Neither the lower court nor the Court of Appeals went so far as to assert that sovereign immunity is a bar to every counterclaim, but restricted those permitted by saying that "counterclaims may not be asserted against a friendly foreign sovereign unless they are based on the subject matter of the suit" (R. 38). The courts below considered the phrase "subject matter of the suit" not as an equitable matter but narrowly and limited to, if not wholly synonymous with, "compulsory counterclaims" as that phrase is defined in Rule 13 of the Federal Rules of Civil Procedure. However, in justification for permitting any counterclaim whatever, in spite of an assertion of sovereign immunity, the District Court reverted to equitable considerations, saying at page 767:

> ". . . When the counterclaim is based on the same subject matter the court may say that the sovereign 'has waived immunity' or 'consented to suit'. These are legal fictions based on the notion that it would be exceedingly inequitable to allow any plaintiff to function as a normal litigant when it is to its advantage to do so, but to raise the shield of sovereign immunity with respect to the same matter, when the tides are turned against it . . ." (R. 38).

But, if this rule be based upon equitable considerations, as indeed it must be, then petitioner fails to see the distinction made by the District Court and affirmed by the Court of Appeals which permitted the sovereign "to raise the shield of sovereign immunity . . . when the tides are turned against it" by reason of petitioner's demand for an offset of debts it owes, but desires to avoid. If recourse must be had to legal fictions in order to imply consent by the sovereign, when equity so demands, then the legal fictions should be invoked to import consent by the

sovereign in this case. Lack of express consent should not protect a sovereign in unconscionable repudiation of it debts to the petitioner while using our courts to enforce a debt, to the further damage of the petitioner.

Specification of Errors to Be Urged

The Circuit Court of Appeals erred (1) in holding that a right of counterclaim (set-off) against a foreign sovereign is limited to the "subject matter of the suit"; (2) in holding that the counterclaims here were not based on the "subject matter of the suit"; (3) in holding that the first counterclaim should not be considered, as a matter of law, "payable at the office of the City Bank"; (4) in holding that the second counterclaim, as a matter of law, should not be considered as "payable at the office of the City Bank"; (5) in defining the phrase "subject matter of the suit" and similar phrases as the basis for inclusion or exclusion of any particular counterclaim as against a sovereign, as of no greater scope than the phrase "subject matter of the opposing party's claim" as used for other purposes in Rule 13 of the Federal Rules of Civil Procedure; and (6) in holding that the announced policy of the State Department in dealing with friendly foreign sovereigns as voluntary litigants in our courts, viz. it had abandoned the classical or "virtual absolute theory of sovereign immunity" and "adopted a restrictive theory of sovereign immunity", did not prevent the dismissal of the counterclaims here.

Reasons for Granting the Writ

The questions presented by this case have fundamental and far-reaching effects upon the present position of the United States in relation to other countries in the world. Their significance may conveniently be grouped under three general considerations:

(1) The authoritative analysis of the rights of a friendly foreign sovereign as a litigant in our courts

is essential to sound and friendly international relations. The concept of sovereignty has peculiar significance at this time, and because of this country's dominant political status in the world and its position as the greatest creditor nation, this Court, by its decision, may well determine that the vast governmental obligations now being assumed throughout the world will not be lightly repudiated.

(2) A decision of this Court is necessary because a state of confusion now exists in this field of the law. This confusion should be resolved for the better administration of justice where friendly foreign sovereigns are before our courts.

(3) A further reason for determination by this Court lies in the disjuncture between judicial interpretation of sovereign rights and the executive determination of what these should be in its foreign relations. Here the State Department has made a very complete and liberal statement of its position[1] and the Court of Appeals has recognized that this position has not been reflected in judicial decisions. Whether or not it should be, the Court of Appeals has said should be left to Congress or the Supreme Court. This Court is the proper forum to make those decisions, because the matter relates to judicial determination of the rights of friendly foreign sovereigns. Since the inception of the Republic such determination has been the prerogative of this Court.

There are other questions of importance in this case, but they are collateral and of less significance than the main issue relating to the attributes of sovereignty. However, it is hoped that, should this Court review the decision of the Court of Appeals, as here requested, it may take occasion to eliminate the doubts created by the opinion of the Court of Appeals as to the relation, under the Federal Reserve Act, of a branch of a national bank to its head office.

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[1] Letter from Acting Legal Adviser Jack B. Tate, dated May 19, 1952, to Acting Attorney General Philip B. Perlman (XXVI, Dept. of State Bull., pp. 984-985 (June 23, 1952)). Appendix D, *post*, p. 20.

Amplifying the first of the three considerations listed above, it should be observed that, at an early time in the history of the United States, this Court had occasion to deal with the question of property seized by a citizen and claimed by a friendly foreign sovereign.[1] Chief Justice Marshall at that time (1812) found no reliable precedent and drew, as he said, his postulates from general principles, and based his conclusions on the situation of the United States in relation to other countries of the world at that time. He determined that the sovereigns of the world, though of equal independence,

> ". . . whose mutual benefit is promoted by intercourse with each other, and by an interchange of those good offices which humanity dictates and its wants require, . . . have consented to a relaxation in practice, in cases under certain peculiar circumstances, of that absolute and complete jurisdiction within their respective territories which sovereignty confers" (p. 136).

The position of friendly foreign sovereign litigants should now be reviewed using these same basic principles, because conditions since that early date have so radically changed. In 1812 the United States had just begun its expansion westward from the Atlantic shore. It was politically weak; it was economically poor. Its military might was negligible, and it was a newcomer in the family of nations. It needed recognition of its rights as a nation. It required vast foreign investments for the development of its resources. It needed to avoid continental wars. One hundred and forty years have changed the circumstances and with it the functions and definition of sovereignty. Economic thinking is no longer *laissez-faire*. The United States no longer is dependent upon foreign capital for its development (although foreign investment is still welcome). It has itself become the greatest lending country in the world, and both from our Government

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[1] *The Schooner Exchange* v. *M'Fadden and Others*, 7 Cranch 116.

and from individuals, friendly foreign governments have borrowed for their economic development.

The United States stands with vast potential powers as to other countries but with no hegemony over the territory of any other. It is in a position to determine by its leadership and example the degree of responsibility which should be assumed by sovereigns voluntarily if they will, imposed on them if necessary, in those economic aspects involving the welfare of its people. The nexus between a decision in this case, and problems yet to arise under the Point IV program, is obvious.

The authoritative determination of this whole doctrine is made more necessary by our second reason for the granting of a writ, which is the confusion that now exists in legal concept, with the result that courts are not always sure to give consistent opinions and have, while giving lip service to some of the old doctrines, nevertheless, in the interests of equity and justice, found exceptions. The obvious and direct injustices resulting from absolute sovereign immunity have been consistently criticized by commentators[1] and from the bench.[2]

For example, in 1946, Mr. Justice Frankfurter, dissenting in *Kennecott Copper Corporation* v. *State Tax Commissioner*, 327 U. S. 573, 580, 581, said:

> "Even while the Civil War was raging Lincoln deemed it important to ask Congress to authorize the Court of Claims to render judgments against the Government. He did so on the score of public morality. 'It is,' wrote Lincoln in his First Annual Mes-

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[1] Paley, "Moral and Political Philosophy"; Laski, "The Responsibility of the State in England", 32 Har. L. Rev. 447 (1919); Borchard, "Government Liability in Tort", 34 Yale L. Jr. 1, 129, 229; 36 Yale L. Jr. 1, 757, 1039; Pugh "Doctrine of Sovereign Immunity", 13 La. L. Rev. 476.

[2] Mr. Justice Wilson in *Chisholm, Executor* v. *Georgia*, 2 Dall. 419, 471, 472, Judge Frank in *Wallace* v. *United States*, 142 F. 2d 240, 243 (C. A. 2).

> sage, 'as much the duty of Government to render prompt justice against itself in favor of citizens as it is to administer the same between private individuals. The investigation and adjudication of claims in their nature belong to the judicial department.' 7 Richardson, Messages and Papers of the Presidents, 3245, 3252. Both the United States and the States are immune from suit unless they agree to be sued. Though this immunity from suit without consent is embodied in the Constitution, it is an *anachronistic survival of monarchical privilege, and runs counter to democratic notions of the moral responsibility* of the State. (Italics supplied.)
>
> "Not so long ago this Court acted on the realization that 'the present climate of opinion . . . has brought governmental immunity from suit into disfavor.' *Keifer & Keifer* v. *R. F. C.*, 306 U. S. 381, 391. . . ."

And, in the case of *United States* v. *Shaw*, 309 U. S. 495, 501 the Court hit at this vestigial remnant of monarchical government. Mr. Justice Reed writing for the Court said:

> ". . . A sense of justice has brought a progressive relaxation by legislative enactment of the rigor of the immunity rule. As representative governments attempt to ameliorate inequalities as necessities will permit, prerogatives of the government yield to the needs of the citizen . . ."

Congress has recognized that a doctrine of immunity is indeed antipathetical to a democratic society and, by various enactments and through the approval of international agreements, has purposefully deprived our Government of immunity in most fields of law, wherever a private party might be exposed to liability.[1]

Since the present case does not envisage the sovereign as a defendant or the subjection of a sovereign's property to seizure, the problem may be confined solely to situations where the sovereign has voluntarily entered the courts of

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[1] See the Federal Tort Claims Act of 1946, 60 Stat. 843, 28 U. S. C. § 1346(b) (1949).

the United States as a litigant, a subject which this Court had occasion to consider in 1937 and, after observing the general proposition, stated[1] by Mr. Justice Stone:

> ". . . But very different considerations apply where the foreign sovereign avails itself of the privilege, likewise extended by comity, of suing in our courts. See *The Sapphire*, 11 Wall. 164, 167; *Russian S. F. S. Republic* v. *Cibrario*, 235 N. Y. 255; 139 N. E. 259. By voluntarily appearing in the role of suitor it abandons its immunity from suit and subjects itself to the procedure and rules of decision governing the forum which it has sought. . . ."

Salutary as this pronouncement was, it would appear that it now needs further emphasis as well as amplification by this Court to become a rule of decision in the lower Federal and in the State courts of our country, for, if this Court intended the principle to be broadly followed, other courts have not so construed it. The doctrine permitting counterclaims, it is believed, should not only be applied here, but by the pronouncement of this Court, should become universally accepted.

In matters of admiralty, this progression is already well apparent as, for example, in *The Gloria, The Thekla, The F. J. Luckenbach, Kingdom of Norway* v. *Federal Sugar Refining Co.*, 286 Fed. 188, at page 194, the court said:

> "There is no principle of public law exempting a sovereign state from its obligations under the law. It should not be assumed that a state desires to deny or evade its obligations. There may be sound reasons of public policy why a state should be immune from the harassment of litigation in forums and under conditions not agreeable to the state. But, once the state has chosen its forum, there seems little reason in law or policy why it should not be subject to the substantive requirements of law and justice."

Other courts have felt as strongly in commercial actions such as in the above mentioned case involving shipping.

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[1] *Guaranty Trust Co.* v. *United States*, 304 U. S. 126, 134.

We quote the language of the opinion in the case of *State of Russia* v. *Bankers Trust Co.*, 4 F. Supp. 417, 420, in which the District Court said:

> "The plaintiff urges its sovereignty as a bar to offsetting the notes against its claim for the credit balance, on the ground that the two causes of action are entirely unconnected. Assuming for the moment that there is no one else interested in the result, it would seem to me inequitable to direct the defendant to pay its debt to the plaintiff when there is a counter debt of far larger amount justly due to the defendant for which it has no remedy. The plaintiff's sovereignty protects it from independent suit, and, furthermore, its property in this country amounts to only a very small part of its indebtedness here, so that, if the offset is barred, the defendant has no remedy whatever. It would be a little too much like tying a defendant hand and foot and letting a plaintiff go through his pockets, and the fact that the plaintiff is a sovereign state does not completely satisfy the moral sense. Concededly the sovereignty of the plaintiff would not protect it from an offset arising out of the same transaction, and it is impossible for me to distinguish the two situations on principles of justice apart from legalisms. In neither case is the defendant obliged in good conscience to pay what the plaintiff demands, even though the law for its own purposes analyzes the relations into a debt owed by the defendant and a counter debt owed to it. This separation may have importance when the rights of third parties intervene or where the defendant has an adequate remedy apart from an offset; but, in the absence of those circumstances, a decree directing the defendant to pay would be shocking to the moral sense, even though the plaintiff is a sovereign state."

And like considerations may be found in the case of *French Republic* v. *Inland Nav. Co.*, *supra*, p. 2n.

It is, therefore, the time for this Court to sweep away those curious concepts which support an outmoded and confused theory of sovereignty, and lay down principles which in succeeding cases may be consistently followed.

The third consideration may be stated very briefly,

namely, that political relations between the United States and other sovereigns are changing. This change has been set forth in detail in the letter from the Acting Legal Adviser of the State Department,[1] in which he succinctly points out that there are two lines of definition of the theory of sovereignty and indicates that the United States will hereafter recognize the restrictive and not the absolute. In so stating the policy for the United States, he pointed out that most of our allies adhere to or are tending towards this restrictive theory, and only those with a different philosophy as to private property have continued the full acceptance of the absolute theory. The State Department is careful to point out that this shift of policy by the Executive Branch cannot control the courts, but, as the granting of sovereign immunity to a foreign litigant is to a large extent a matter of proper relations within the family of nations, this shift of policy is clearly a reason why this Court should reconsider the position of a friendly foreign sovereign as a litigant.

In deciding these momentous questions, the Court will determine the jurisdiction of the District and Circuit Courts, for here the District Court declined jurisdiction of the counterclaims of the defendant, but continues to entertain the suit against it. Clearly, in such a case justice, as known, between private persons, cannot be done, although there is complete privity between the parties involved.

The case is not an isolated one. This very sovereign has, within the past few years, commenced six cases against American Corporations, three of them against this petitioner.[2] Other demands and claims are pending;

[1] Letter from Acting Legal Adviser Jack B. Tate, *post*, p. 20.

[2] *Republic of China* v. *American Express Co.*, 195 F. 2d 230; *Bank of China* v. *Wells Fargo Bank & Union Trust Co.*, 190 F. 2d 1010; *Chase Nat. Bank of City of N. Y.* v. *Directorate General of Postal Remittances & Savings Bank et al.*, 112 N. Y. S. 2d 14; *Republic of China (Postal Remittances)* v. *The National City Bank*, D. C. S. D. N. Y. Docket No. 78-288; *Republic of China* v. *The National City Bank*, D. C. S. D. N. Y. Docket No. 79-23.

and, as governments become more and more concerned with the economic life of their nation, more frequently will they appear as litigants. The problems here presented are, therefore, recurring ones which are sure to arise in increasing numbers. An authoritative definition by this Court is required to protect all who do business with a foreign government and to maintain the significance of American justice.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that a Writ of Certiorari be granted.

Respectfully submitted,

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March 1, 1954.

APPENDIX A

Section 25 of the Federal Reserve Act, 12 U. S. C. Section 604.

"Every national banking association operating foreign branches shall conduct the accounts of each foreign branch independently of the accounts of other foreign branches established by it and of its home office, and shall at the end of each fiscal period transfer to its general ledger the profit or loss accrued at each branch as a separate item. Dec. 23, 1913, c. 6, § 25, 38 Stat. 273; Sept. 7, 1916, c. 461, 39 Stat. 755."

APPENDIX B

Section 147 of the New York Negotiable Instruments Law.

"Where the instrument is made payable at a bank it is equivalent to an order to the bank to pay the same for the account of the principal debtor thereon."

APPENDIX C

Rule 13(a) of the Federal Rules of Civil Procedure.

"(a) *Compulsory Counterclaims.* A pleading shall state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party's claim and does not require for its adjudication the presence of third parties of whom the court cannot acquire jurisdiction, except that such a claim need not be so stated if at the time the action was commenced the claim was the subject of another pending action. As amended Dec. 27, 1946, effective March 19, 1948."

APPENDIX D

Letter from Acting Legal Adviser Jack B. Tate, dated May 19, 1952, to Acting Attorney General Philip B. Perlman (XXVI, Department of State Bulletin, pp. 984-985 (June 23, 1952)).

My dear Mr. Attorney General:

The Department of State has for some time had under consideration the question whether the practice of the Government in granting immunity from suit to foreign governments made parties defendant in the courts of the United States without their consent should not be changed. The Department has now reached the conclusion that such immunity should no longer be granted in certain types of cases. In view of the obvious interest of your Department in this matter I should like to point out briefly some of the facts which influenced the Department's decision.

A study of the law of sovereign immunity reveals the existence of two conflicting concepts of sovereign immunity, each widely held and firmly established. According to the classical or absolute theory of sovereign immunity, a sovereign cannot, without his consent, be made a respondent in the courts of another sovereign. According to the newer or restrictive theory of sovereign immunity, the immunity of the sovereign is recognized with regard to sovereign or public acts (*jure imperii*) of a state, but not with respect to private acts (*jure gestionis*). There is agreement by proponents of both theories, supported by practice, that sovereign immunity should not be claimed or granted in actions with respect to real property (diplomatic and perhaps consular property excepted) or with respect to the disposition of the property of a deceased person even though a foreign sovereign is the beneficiary.

The classical or virtually absolute theory of sovereign immunity has generally been followed by the courts of the

United States, the British Commonwealth, Czechoslovakia, Estonia, and probably Poland.

The decisions of the courts of Brazil, Chile, China, Hungary, Japan, Luxembourg, Norway, and Portugal may be deemed to support the classical theory of immunity if one or at most two old decisions anterior to the development of the restrictive theory may be considered sufficient on which to base a conclusion.

The position of the Netherlands, Sweden, and Argentina is less clear since although immunity has been granted in recent cases coming before the courts of those countries, the facts were such that immunity would have been granted under either the absolute or restrictive theory. However, constant references by the courts of these three countries to the distinction between public and private acts of the state, even though the distinction was not involved in the result of the case, may indicate an intention to leave the way open for a possible application of the restrictive theory of immunity if and when the occasion presents itself.

A trend to the restrictive theory is already evident in the Netherlands where the lower courts have started to apply that theory following a Supreme Court decision to the effect that immunity would have been applicable in the case under consideration under either theory.

The German courts, after a period of hesitation at the end of the nineteenth century have held to the classical theory, but it should be noted that the refusal of the Supreme Court in 1921 to yield to pressure by the lower courts for the newer theory was based on the view that that theory had not yet developed sufficiently to justify a change. In view of the growth of the restrictive theory since that time the German courts might take a different view today.

The newer or restrictive theory of sovereign immunity has always been supported by the courts of Belgium and Italy. It was adopted in turn by the courts of Egypt and

of Switzerland. In addition, the courts of France, Austria, and Greece, which were traditionally supporters of the classical theory, reversed their position in the 20's to embrace the restrictive theory. Rumania, Peru, and possibly Denmark also appear to follow this theory.

Furthermore, it should be observed that in most of the countries still following the classical theory there is a school of influential writers favoring the restrictive theory and the views of writers, at least in civil law countries, are a major factor in the development of the law. Moreover, the leanings of the lower courts in civil law countries are more significant in shaping the law than they are in common law countries where the rule of precedent prevails and the trend in these lower courts is to the restrictive theory.

Of related interest to this question is the fact that ten of the thirteen countries which have been classified above as supporters of the classical theory have ratified the Brussels Convention of 1926 under which immunity for government owned merchant vessels is waived. In addition the United States, which is not a party to the Convention, some years ago announced and has since followed, a policy of not claiming immunity for its public owned or operated merchant vessels. Keeping in mind the importance played by cases involving public vessels in the field of sovereign immunity, it is thus noteworthy that these ten countries (Brazil, Chile, Estonia, Germany, Hungary, Netherlands, Norway, Poland, Portugal, Sweden) and the United States have already relinquished by treaty or in practice an important part of the immunity which they claim under the classical theory.

It is thus evident that with the possible exception of the United Kingdom little support has been found except on the part of the Soviet Union and its satellites for continued full acceptance of the absolute theory of sovereign immunity. There are evidences that British authorities are aware of its deficiencies and ready for a change. The reasons which obviously motivate state trading countries

in adhering to the theory with perhaps increasing rigidity are most persuasive that the United States should change its policy.

Furthermore, the granting of sovereign immunity to foreign governments in the courts of the United States is most inconsistent with the action of the Government of the United States in subjecting itself to suit in these same courts in both contract and tort and with its long established policy of not claiming immunity in foreign jurisdictions for its merchant vessels. Finally, the Department feels that the widespread and increasing practice on the part of governments of engaging in commercial activities makes necessary a practice which will enable persons doing business with them to have their rights determined in the courts. For these reasons it will hereafter be the Department's policy to follow the restrictive theory of sovereign immunity in the consideration of requests of foreign governments for a grant of sovereign immunity.

It is realized that a shift in policy by the executive cannot control the courts but it is felt that the courts are less likely to allow a plea of sovereign immunity where the executive has declined to do so. There have been indications that at least some Justices of the Supreme Court feel that in this matter courts should follow the branch of the Government charged with responsibility for the conduct of foreign relations.

In order that your Department, which is charged with representing the interests of the Government before the courts, may be adequately informed it will be the Department's practice to advise you of all requests by foreign governments for the grant of immunity from suit and of the Department's action thereon.

Sincerely yours,

For the Secretary of State:

JACK B. TATE
Acting Legal Adviser

Brief for the Petitioner

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1954

No. 30

THE NATIONAL CITY BANK OF NEW YORK,
Petitioner,

v.

THE REPUBLIC OF CHINA,
Respondent,

and

THE SHANGHAI-NANKING RAILWAY ADMINISTRATION, MOH HAN, as Director of the Shanghai-Nanking Railway Administration, SAU CHEN, as Deputy Director of the Shanghai-Nanking Railway Administration,
Plaintiffs.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1954

No. 30

THE NATIONAL CITY BANK OF NEW YORK,
Petitioner,

v.

THE REPUBLIC OF CHINA,
Respondent,

and

THE SHANGHAI-NANKING RAILWAY ADMINISTRATION, MOH HAN, as Director of the Shanghai-Nanking Railway Administration, SAU CHEN, as Deputy Director of the Shanghai-Nanking Railway Administration,
Plaintiffs.

BRIEF FOR PETITIONER, THE NATIONAL CITY BANK OF NEW YORK, ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

Opinions Below

The opinion of the District Court for the Southern District of New York granting the motion by The Republic of China to dismiss two counterclaims (R. 35) is reported in 108 F. Supp. 766. The opinion of the District Court denying defendant's motion for reargument and for leave to amend the counterclaims (R. 55) is reported in 14 F. R. D. 186. The opinion of the Court of Appeals (R. 64) affirming the District Court, is reported at 208 F. 2d 627.

Jurisdiction

The judgment of the Court of Appeals was entered on December 8, 1953 (R. 71). The defendant's petition for a writ of certiorari was filed March 2, 1954, and was granted April 26, 1954 (R. 72). The jurisdiction of this Court rests on 28 U. S. C., Section 1251 (1).

Statutes Involved

The statutes cited or relied upon, relevant to this case are: (1) Section 25 (b) of the Federal Reserve Act (Title 12, U. S. C., Section 632); (2) Section 25 of the Federal Reserve Act (Title 12, U. S. C., Section 604); (3) Section 147 of the New York Negotiable Instruments Law; (4) Rule 13 of the Federal Rules of Civil Procedure.

The pertinent texts are set forth in Appendix A, *infra*, page i.

Question Presented

The question presented is the extent to which a foreign government which institutes an action in the courts of the United States against an American corporation to recover a debt may rely on the doctrine of "sovereign immunity" to avoid a defense to the action, asserted by way of counterclaim, based on a debt owed by it to the defendant. To take the precise situation which exists in this case is: Can a foreign government which has borrowed money from an American bank and is in default on the loan sue the bank for the balance in a deposit account and recover a judgment for the entire balance, regardless of its indebtedness to the bank?

Statement

On December 21, 1948, The National City Bank of New York, the defendant herein (hereinafter referred to as "City Bank"), received at its head office in New York City from its Shanghai Branch $200,000 to create a new account in the name of the Shanghai-Nanking Railway Administration (R. 13). Thereafter demands for payment of this account were made upon the City Bank by several persons, some of whom are not parties to the action. The City Bank refused to comply with any of these demands (R. 14-16).

This action was commenced on May 2, 1951 to recover the balance of $200,000 in the said account (R. 3). The plaintiff, The Republic of China, alleged that the Shanghai-Nanking Railway Administration was an agency of the Ministry of Communications of The Republic of China and that the individual plaintiffs were officials of such agency (R. 4). In view of the adverse claims which had been presented to the City Bank with respect to the account, the defendant invoked § 51-a of the Civil Practice Act of the State of New York, a procedure provided as protection against adverse claimants where interpleader is not possible because of lack of jurisdiction of the adverse claimants, and obtained a stay of the action until June 30, 1952, for the purpose of permitting adverse claimants to come in.

On July 11, 1952 the City Bank served its amended answer, containing denials and affirmative defenses and also two counterclaims asserted to defeat the action of the plaintiff, The Republic of China (R. 11).

The first counterclaim (R. 23) alleges that, in 1920, the City Bank participated in a $5,000,000 loan to the Pacific Development Company which was secured by a $5,500,000

Chinese Government Treasury Note. This note was the direct obligation of The Republic of China, respondent here, and was payable in New York at one of the member banks of the loaning syndicate. The loan was not paid on its maturity date and upon the liquidation of the Pacific Development Company in 1928 the note was reduced to possession by J. P. Morgan & Co. on behalf of the banks which participated in the loan, by the purchase and sale of this obligation at public auction. This note of the plaintiff is now held by one of the member banks of the syndicate for the benefit of all. The City Bank has a participating interest in the amount of $317,720.93 plus interest, no part of which has been paid, although this indebtedness has been recognized by The Republic of China.

The second counterclaim (R. 25) alleges that, in 1947 and 1948, the City Bank made further loans to The Republic of China by means of the purchase of Chinese Government 36th Year short-term Treasury Notes (commemorative of the 36th Year of the establishment of the Republic). These Notes were purchased through the Shanghai Branch of the City Bank and were payable at the Central Bank of China or at any of its appointed banks, among which were the Shanghai and other Far Eastern branches of the City Bank (R. 32). Some of these obligations were paid, but there remains the unpaid amount equal to the sum of $391,033.60, with interest, for which The Republic of China is indebted to the City Bank.

On September 15, 1952, The Republic of China moved (R. 34) pursuant to Rule 12 of the Federal Rules of Civil Procedure to dismiss the counterclaims on the grounds:

"1. That the Court lacks jurisdiction thereof because plaintiff The Republic of China is a friendly sovereign which has not consented to be sued on the matters therein alleged.

"2. That they fail to state claims against plaintiff The Republic of China upon which relief can be granted."

On December 22, 1952, Hon. Irving R. Kaufman, District Judge for the Southern District of New York, granted the motion to dismiss the counterclaims (R. 41). The court said (R. 38): "it is well settled that counterclaims may not be asserted against a friendly foreign sovereign unless they are based on the subject matter of the suit", and held that the counterclaims here did not "arise out of the same subject matter covered in the complaint", citing *United States* v. *New York Trust Co.*, 75 F. Supp. 583 (D. C. S. D. N. Y. 1946); and *Republic of China* v. *American Express Co.*, 195 F. 2d 230, 233 (C. A. 2, 1952).

On January 22, 1953, the City Bank moved (R. 46) for reargument and for leave to amend the counterclaims in order to indicate clearly that the counterclaims were not intended to achieve affirmative relief against The Republic of China, but merely to defeat the plaintiff's efforts to compel the defendant bank to pay $200,000 to it, and that all the Chinese Treasury Notes in both counterclaims were payable at the City Bank within the meaning of § 147 of the New York Negotiable Instruments Law. This motion was denied (R. 55).

An appeal was taken to the Court of Appeals for the Second Circuit, which affirmed the orders of the District Court by judgment entered December 8, 1953 (R. 71). Judge Frank, in delivering the opinion, stated that, for the purpose of the appeal, the court considered the counterclaims as if they had been amended in the manner proposed by the defendant in its motion for leave to amend (R. 67). In expressing his reasons for affirming the decision of the lower court, he said (R. 67-8):

". . . We think the trial judge correctly held that

the counterclaims here were not based on the subject matter of the suit. We reach the same result if we regard the counterclaims as but set-offs. For the assertion against a sovereign government of a counterclaim or set-off, unrelated to the claim asserted by the sovereign in its suit, is the equivalent of an independent suit against that sovereign brought without its consent. Wherefore we think the district court's orders were correct." (Citing *In re Monongahela Rye Liquors*, 141 F. 2d 864, 869 (C. A. 3).)

He added significantly (R. 68):

". . . We have no high regard for the idea that, without its consent, a government may not be sued for acts which, if done by a private person, would be actionable wrongs. But we feel that we must leave to Congress or the Supreme Court any marked diminution of that hoary doctrine (although, in the belief of many persons, it is basically immoral)."

Summary of Argument

The Republic of China owes the City Bank more than $700,000, plus interest. It has brought this action to recover a $200,000 bank account held by City Bank in the name of The Shanghai-Nanking Railway Administration. In its amended answer to the complaint, City Bank set forth two counterclaims based on the large indebtedness to it from The Republic of China. Although this indebtedness far exceeds the amount claimed by The Republic of China, the City Bank does not seek any affirmative relief, but desires merely to defeat plaintiff's action.

The court below pointed out, as other courts have done, that, because of comity and international goodwill, a friendly foreign sovereign may not be sued in our courts without its consent. But when a sovereign voluntarily

comes into our courts seeking their aid in a controversy against a person or domestic corporation of this country, the sovereign impliedly waives its immunity and consents to the imposition against it of defenses, set-offs, counterclaims and other forms of pleading available to the defendant, as though the sovereign were a private litigant. Courts have always been careful to say, however, that this consent of the sovereign is "implied". This is the important word, for it is the law which creates the consent and not an affirmative expression of consent by the foreign sovereign itself. So the law determines consent—"implied" consent—of the sovereign where it finds this to be required by equity and justice and, of course, such consent is found even though the sovereign in any particular case may affirmatively object.

Some lower Federal courts, however, have put a limitation on the type of counterclaim which is permitted against a foreign sovereign. Those lower courts state that only counterclaims which arise out of the subject matter of the action may be imposed against a sovereign without its express consent. As authority for such a limitation those courts have relied upon several decisions of this Court. It is submitted that these Supreme Court decisions in no way stand for the proposition for which they are cited. To the contrary, a more reasonable interpretation would indicate that they represent, in the first instance, a remission from the ancient and rigid rule of sovereign immunity. Some of these Supreme Court cases dealt with situations where to exclude a counterclaim which was immediately, obviously and necessarily connected with, and growing out of, the same transaction which the plaintiff sued upon, such as is found in admiralty actions for example, would so shock the conscience of the Court that it naturally assumed that the sovereign involved had consented to have such a counterclaim considered. Thus, these decisions are in reality a withdrawal from the doctrine of sovereign immunity. They expose

the sovereign to liability where before none was permitted. They do not even by implication indicate any limitation imposed on the scope of a counterclaim to be permitted against a foreign sovereign. They should be considered as favoring consideration of all equitable matters existing between the parties; and the categories of counterclaims permitted against a foreign sovereign should, as equity may require, be enlarged.

The decisions of the lower courts in this case excluding the counterclaims are wholly empirical or, at best, based upon decisions of other courts which have made this same erroneous interpretation. There is absolutely no authoritative precedent for such a limitation on the kind of counterclaim which may be pleaded against a foreign sovereign. This Court has never made any pronouncement on the subject. There is no reason, either as a matter of comity or public policy, why a defendant, when sued in our courts by a foreign government, should be so restricted in the methods he may use to defend himself. If the defendant may not in any event obtain an affirmative judgment against the sovereign, without its consent, there is no danger of interference with essential governmental activities by permitting counterclaims of wide scope against the sovereign; and the fact that it is the sovereign itself which has brought the suit precludes any consideration of comity or preservation of "dignity".

The doctrine of sovereign immunity is an anachronism. Most of the civilized countries of the world have drastically restricted its application. The legislative branch of our own government has enacted laws enabling our citizens to bring suit against the United States in the Court of Claims and, at a very early date, enacted a statute providing for offsets or "credits". In suits brought by the United States, counterclaims such as those pleaded in this case would be permitted by way of offset. Many

foreign governments have restricted the doctrine of sovereign immunity as applied to themselves and, also, to other foreign sovereigns suing in their courts; and our State Department has indicated that it favors restrictions on the doctrine of sovereign immunity when invoked by foreign governments. It is time for our courts to reexamine the doctrine of soverign immunity as applied to foreign governments so that resort to that doctrine may no longer be a means of defeating the ends of justice.

The lower court here found, for reasons not wholly explicit, that there must be a direct connection between the claim asserted in the complaint and any permissible counterclaim. This assumption was based upon its acceptance of the proposition that some limitation on the scope of counterclaims against a sovereign was proper. Even adopting such a limitation, it is the contention of the petitioner that the counterclaims here under consideration *did* arise out of the same "transaction" which is the subject matter of the action. The Republic of China and the City Bank have had banking relationships with each other for many years and the debts which are the subject of the counterclaims are incidents of this long association.

The action by the plaintiff is to collect from the defendant bank a bank account established by transfer of funds from Shanghai, China, in 1948 (R. 13), the very year in which the defendant advanced funds in Shanghai, China, to the plaintiff in even greater amount. Unpaid portions of funds previously advanced both in Shanghai and in New York were outstanding. Thus, the obligations of the plaintiff to the defendant are part of a long chain of events logically connected, one link of which is the basis for the plaintiff's claim against the defendant. Under the broad interpretation which has been given to the word "transaction" in construing Rule 13 (a) of the Federal Rules of Civil Procedure, and in accordance with the fundamental purpose of Rule 13 to settle in so far

as possible all disputes between the litigants at one trial, these counterclaims are proper and should be allowed.

Presentation of Argument

The court here adopted two postulates which it held to be fixed rules of law binding upon it. These were: that a foreign sovereign impliedly consents only to counterclaims arising out of the subject matter of the action, and the other: that a foreign sovereign may not be sued in the courts of the United States without its consent.

The petitioner's brief will, in Points I, II and III, show that the first assumption above mentioned is not binding in this case, or even tenable, for there is no precedent for the limitation of a counterclaim against a foreign sovereign to the subject matter of the action; that, even if such limitation exists, the counterclaims here pleaded are within that limitation; and that, in construing the proposition, the lower courts applied it too broadly.

The petitioner, in Point IV, will show that, even accepting the restrictions adopted by the courts below, the counterclaims here come within well defined exceptions.

In Point V, it will be shown that the second proposition which the Court of Appeals felt binding upon it, that a sovereign may not be sued without its consent, is not controlling in this case; "consent" of a sovereign is always an "implied consent", and the plaintiff here is not immune from liability.

POINTS

I

There is no reason why a counterclaim against a foreign sovereign should be limited to the subject matter of the action and there is no authoritative precedent for such limitation.

The City Bank and The Republic of China have had business relations with each other for years. Since 1920 the City Bank has made loans secured by Chinese Treasury Notes, the unpaid balance of which now amounts to more than $700,000. These loans were made in good faith, but The Republic of China, although it acknowledges its indebtedness, has defaulted on its obligations. Several demands for payment have been made, but rejected.

Now, The Republic of China has come into our courts seeking payment of a $200,000 account held by the City Bank in the name of an agency of that government. In an effort to minimize its losses, the City Bank has attempted to prevent this recovery by asserting, as counterclaims, the indebtedness owed to it by the plaintiff. The City Bank does not seek an affirmative judgment against The Republic of China,[1] but raises the counterclaims merely as a defense to the action. Whether such a pleading be called a set-off, recoupment or counterclaim, its purpose is to defeat a recovery by the plaintiff.[2] In re-

[1] It is conceded for present purposes that affirmative relief cannot be granted against a sovereign without its consent. *De Groot* v. *U. S.*, 5 Wall. 419; *United States* v. *Shaw*, 309 U. S. 495; *French Republic* v. *Inland Nav. Co.*, 263 Fed. 410.

[2] It should be pointed out that much of the confusion existent in this field arises from indiscriminate use of the words "recoupment", "set-off" and "counterclaims". Today under the Federal Rules, all claims brought by a defendant against the op-

sponse to these counterclaims, The Republic of China endeavors to raise the shield of sovereign immunity, contending that the two counterclaims are in effect separate actions against a friendly foreign sovereign which has not consented to be sued.

If the government of the United States brings an action against a private individual or corporation based on an alleged indebtedness to the government, the defendant may claim as a credit any indebtedness to him from the government, whether or not arising from the same transaction on which the government's claim is based. The courts have so held on numerous occasions in giving effect to legislation originally enacted by the Congress more than a century and a half ago.

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posing party are denominated "counterclaims", and include those claims formerly known as "set-off" and "recoupment". See Federal Rules of Civil Procedure § 13 and Moore's Federal Practice, Vol. 3, § 13.02. The meanings of these terms are still significant in studying early cases, however, and it is especially important to bear in mind the differences between these remedies in the cases here examined.

Recoupment was a defense at common law which permitted a defendant "to show for the purpose of reducing the plaintiff's recovery any facts arising out of the transaction sued upon or connected with the subject thereof which facts might have founded an independent action in favor of the defendant against the plaintiff". Clark on Code Pleading § 100.

Set-off was originally an equitable remedy which allowed the defendant to raise claims arising out of transactions independent of those sued upon. Later, a statutory set-off was permitted at law. Clark on Code Pleading, *ibid.* "The right of set-off is based on principles of right, justice and benevolence" and these broad equitable principles may be applied both at law and in equity. 80 C. J. S. 8.

"Counterclaim, which is a creation of statute and did not exist at common law, is frequently more extensive than set-off or recoupment, or it is the equivalent of the two combined, or includes them both." 47 Am. Jur. 709. Under earlier State Codes counterclaims were usually limited to the subject matter of the action. Clark on Code Pleading, *ibid.*

"In this brief all such claims will be called 'counterclaims' in accordance with the Federal Rules."

U. S. v. *Wilkins*, 6 Wheat. 135, 144;
Watkins v. *U. S.*, 9 Wall. 759;
U. S. v. *Buchanan*, 8 How. 83;
U. S. v. *Eckford*, 6 Wall. 484, 491;
U. S. v. *Shaw*, 309 U. S. 495, 501-2;
28 U. S. C. § 2406.

It is somewhat startling that a foreign government should be supposed to enjoy immunity from defenses to which the government of the United States is subject. The immunity from suit of the government of the United States has been said on many occasions to be absolute, except where it has expressly consented, by statutory enactment, to be sued. *De Groot* v. *U. S.*, 5 Wall. 419. In the case of foreign governments, however, there has never been legislation by the Congress or by any State legislature defining the nature and extent of the immunity foreign governments should enjoy in our courts. The law on the subject is entirely judge-made; and, in the absense of any definitive pronouncements by this Court, a great deal of confusion has arisen because of various theories adopted by the courts in a great variety of cases involving foreign governments.

In order to avoid unjust or inequitable results in certain cases, the courts have resorted to legal fictions from which they were able to find an "implied consent" by the government involved to have certain claims asserted against it. The most obvious situations in which the courts have found such implied consent have been those involving a single transaction, as to which the rights of both parties must be determined in order to achieve a just result. It is respectfully submitted, however, that there is no sound judicial reason for limiting defenses and counterclaims to the "same transaction."

In a case quite similar to this[1] the District Court for

[1] *State of Russia* v. *Bankers Trust Co.*, 4 F. Supp. 417, 420; aff'd 83 F. 2d 236.

the Southern District of New York, in denying plaintiff's plea of sovereign immunity, said:

> ". . . it would seem to me inequitable to direct the defendant to pay its debt to the plaintiff when there is a counter debt of far larger amount justly due to the defendant for which it has no remedy. The plaintiff's sovereignty protects it from independent suit, and, furthermore, its property in this country amounts to only a very small part of its indebtedness here, so that, if the offset is barred, the defendant has no remedy whatever. It would be a little too much like tying a defendant hand and foot and letting a plaintiff go through his pockets, and the fact that the plaintiff is a sovereign state does not completely satisfy the moral sense. . . ."

It has been the long-accepted rule that, upon principles of comity, a friendly sovereign may not be sued in our courts without its consent.

> *The Schooner Exchange* v. *M'Faddon,* 7 Cranch 116;
> *Beers* v. *Arkansas,* 20 How. 527, 529;
> *Kingdom of Roumania* v. *Guaranty Trust Co.,* 250 Fed. 341;
> *Lyders* v. *Lund,* 32 F. 2d 308.

But this immunity cannot be asserted when a sovereign voluntarily comes into our courts seeking their aid. Comity does not require that our courts render a United States citizen defenseless in an action initiated by a foreign sovereign. As this Court has said:

> "It is true that upon the principle of comity foreign sovereigns and their public property are held not to be amenable to suit in our courts without their consent. See *The Exchange,* 7 Cranch 116; *Berizzi Bros. Co.* v. *S. S. Pesaro,* 271 U. S. 562; *Compania*

Espanola v. *The Navemar*, 303 U. S. 68. But very different considerations apply where the foreign sovereign avails itself of the privilege, likewise extended by comity, of suing in our courts. See *The Sapphire*, 11 Wall. 164, 167; *Russian S. F. S. Republic* v. *Cibrario*, 235 N. Y. 255; 139 N. E. 259. By voluntarily appearing in the role of suitor it abandons its immunity from suit and subjects itself to the procedure and rules of decision governing the forum which it has sought . . ."

Guaranty Trust Co. v. *United States*, 304 U. S. 126, 134.

Thus, a foreign sovereign which comes into our courts impliedly consents to a determination of the controversy, on just and equitable principles.

Republic of China v. *American Express Co.*, (C. C. A. 2d) 195 F. 2d 230;
In re Monongahela Rye Liquors, 141 F. 2d 864;
Cf. Porto Rico Co. v. *Ramos*, 232 U. S. 627;
Veitia v. *Fortuna Estates*, 240 Fed. 256.

As stated by Judge Chase in *Republic of China* v. *American Express Co.* (*supra*) at page 233:

". . . Accordingly, we have held that a sovereign who sues in our courts so submits itself to the jurisdiction it has invoked that defenses by way of set-off and of counterclaim are available against it. *United States* v. *National City Bank of New York*, 2 Cir., 83 F. 2d 236, certiorari denied, 299 U. S. 563, 57 S. Ct. 25, 81 L. Ed. 414; see *Dexter & Carpenter, Inc.* v. *Kunglig Jarnvagsstyrelsen*, 2 Cir., 43 F. 2d 705, 708, certiorari denied, 282 U. S. 896, 51 S. Ct. 181, 75 L. Ed. 789. . . ."

This statement of the law appears just and reasonable; but some of our courts, whether through a misun-

derstanding of earlier cases or through an unconscious application of outmoded principles of pleading, have put a qualification upon this implied consent to suit by counterclaim. It has been said that counterclaims against a sovereign must be based upon the "subject matter" of the suit.

United States v. *New York Trust Co.*, 75 F. Supp. 583;
Republic of China v. *American Express Co.*, (*supra*);
Kingdom of Roumania, 250 Fed. 341.

The authority for this limitation is hazy. For example, in *Republic of China* v. *American Express Co.*, the court cites *The Thekla* (266 U. S. 328) as standing for this proposition. In *The Thekla*, the lower court had entered a decree against the United States for $120,619.71, and the question was whether the District Court was empowered by law to render this decree. In holding that it was, the court stated that since the United States had voluntarily come into the admiralty action as a libelant, justice would be done with regard to the "subject matter". This is obviously a long way from saying that a counterclaim against a foreign government, when interposed by way of defense, must be limited to the subject matter of the suit. *The Thekla* was an admiralty action and decided that, because of the peculiar nature of such actions, complete justice could not be done unless an affirmative judgment was entered against the United States. The reasoning of the court is explained in *United States* v. *Shaw* [309 U. S. 495, 502], as follows:

> "The Thekla turns upon a relationship characteristic of claims for collision in admiralty . . . The subject matter of a suit for damages in collision is not the vessel libelled but the collision. Libels and cross-libels for collision are one litigation and give rise to one liability. In equal fault, the entire dam-

> age is divided. As a consequence when the United States libels the vessel of another for collision damages and a cross-libel is filed, it is necessary to determine the cross-libel as well as the original libel to reach a conclusion as to liability for the collision. That conclusion must be stated in terms of responsibility for damages. . . ."

Thus, *The Thelka* had nothing to do with *what type* of counterclaim may be interposed as a defense but dealt only with the *extent* of its imposition in an admiralty suit. Mr. Justice Holmes expressly indicated that the scope of counterclaims against a sovereign should be a broad one, such as was authorized in equitable set-offs. He said at page 341:

> ". . . the reasons are strong for not obstructing the application of natural justice against the Government by technical formulas when justice can be done without endangering any public interest . . . It is said that there is no statute by which the Government accepted this liability. It joined in the suit, and that carried with it the acceptance of whatever liability the courts may decide to be reasonably incident to that act."

Another case frequently cited[1] as authority for limiting counterclaims against a sovereign to claims arising out of the subject matter of the action is *Bull* v. *United States*, (295 U. S. 247). In that case the Commissioner of Internal Revenue, in 1921, improperly classified $212,718.79 received by the Executor, subsequent to decedent's death, as corpus of the estate and subjected it to estate tax, which the Executor paid. Thereafter, in 1925, the Commissioner determined that this sum of money was income to the estate and subjected it to income tax. The Executor complained that the same sum of money

[1] Cited in *In re Monongahela Rye Liquors*, 141 F. 2d 864 and *United States* v. *New York Trust Co.*, 75 F. Supp. 583.

could not be both corpus and income, and taxed in each capacity. He opposed the payment of this income tax by demanding recoupment[1] of the amount mistakenly collected as estate tax and wrongfully retained. An appeal was taken to the Board of Tax Appeals. The Board sustained the Commissioner. The Executor paid the deficiency in 1928 and filed claim for refund, which was rejected. Suit was brought in the Court of Claims in 1930. The petition alleged that, if the sum of money was properly taxable as income, the United States should have credited the amount paid as estate tax against the deficiency determination of income tax. The Court of Claims rejected this plea "for the reason that the suit was not timely brought".

This Court held that the $212,718.79 was properly classified as income to the estate and taxable as such. The Commissioner's rulings, however, were held to be inconsistent. The identical money could not properly be the basis of two assessments. The Court summarizes the situation as follows (pp. 260-261):

> "In a proceeding for the collection of estate tax, the United States through a palpable mistake took more than it was entitled to. Retention of the money was against morality and conscience. But claim for refund or credit was not presented or action instituted for restitution within the period fixed by the statute of limitations. If nothing further had occurred Congressional action would have been the sole avenue of redress."

Faced with this dilemma the Court asks (p. 259):

". . . Upon what theory, then, may the petitioner

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[1] It should be remembered that recoupment was a common law defense arising out of the transaction upon which plaintiff's action was grounded.

> obtain redress in the present action for the unlawful retention of the money of the estate? . . ."

and gives the answer as follows (p. 261):

> ". . . A claim for recovery of money so held . . . may be used by way of recoupment and credit in an action by the United States arising out of the same transaction. *United States* v. *Macdaniel*, 7 Pet. 1, 16, 17; *United States* v. *Ringgold*, 8 Pet. 150, 163-164. . . ."

Neither of the two cases there cited is authority for the limitation imposed by the Court on the scope of the counterclaims permitted against the government. In fact the *Ringgold* case appears to indicate that there is no limit to the type of claim that can be asserted as a defense to a suit by the United States. The Court says (*United States* v. *Ringgold*, 8 Pet. 163-164):

> ". . . No direct suit can be maintained against the United States. But when an action is brought by the United States, to recover money in the hands of a party who has a legal claim against them, it would be a very rigid principle to deny to him the right of setting up such claim in a court of justice, and turn him round to an application to congress. . . . The government seeks to recover money from the defendant, to which he is equitably entitled for services rendered. This court cannot see any right, either legal or equitable, in the government, to the money, for the recovery of which this action is brought."

It is clear, therefore, that the *Bull* case does not hold that all counterclaims against a sovereign (there, the United States) must arise out of the same transaction as that sued upon. The court was considering claims against a sovereign by way of recoupment only. There was no issue as to the type or scope of such a claim. The fact that the court was confining its opinion to a

consideration of recoupment only is made very clear where it said (p. 262):

> ". . . If the claim for income tax deficiency had been the subject of a suit, any counter demand for recoupment of the overpayment of estate tax could have been asserted by way of defense and credit obtained notwithstanding the statute of limitations had barred an independent suit against the Government therefor. This is because recoupment is in the nature of a defense arising out of some feature of the transaction upon which the plaintiff's action is grounded. Such a defense is never barred by the statute of limitations so long as the main action itself is timely."

Another case sometimes cited[1] as authority for the proposition that a counterclaim against a sovereign must be limited to the subject matter of the action is *The Siren*, (7 Wall. 152). That was an admiralty action in which the United States voluntarily appeared as a libelant. Nowhere is any language to be found sustaining such a proposition. To the contrary, the case holds that, when a sovereign voluntarily comes into court "it waives its exemption and submits to the application of *the same principles by which justice is administered between private suitors*" (p. 159 [emphasis added]). The Court said (p. 154):

> "But although direct suits cannot be maintained against the United States, or against their property, yet, when the United States institute a suit, they waive their exemption so far as to allow a presentation by the defendant of set-offs, legal and equitable, to the extent of the demand made or property claimed, and when they proceed *in rem*, they open to consideration all claims and equities in regard

[1] Cited in *Bull* v. *United States*, 295 U. S. 247 and the *Western Maid*, 257 U. S. 419.

to the property libelled. They then stand in such proceedings, with reference to the rights of defendants or claimants, precisely as private suitors, except that they are exempt from costs and from affirmative relief against them, beyond the demand or property in controversy. . . ."

The proposition that a counterclaim against a sovereign must be limited to the subject matter of the action has, therefore, no authoritative precedent whatever. This Court has never made any pronouncement upon the subject, nor has it ever reviewed any of the lower court decisions espousing such a limitation. The proposition undoubtedly owes its inception to the transposition of language dealing with recoupment, as found in the case of *Bull* v. *United States, supra*, and to principles of code pleading in general, which were formulated in this country around the middle of the last century.

See, *People* v. *Dennison*, 84 N. Y. 272.

Under the Federal Rules of Civil Procedure, where the emphasis is placed on settling as many disputes between the litigants as possible in one trial, there seems little justification for keeping alive the old restrictive forms of pleading. Our courts have long abandoned the theory that it is impossible or unjust to join parties and actions in one law suit when logic and convenience so demand, and our present-day rules of pleading have been liberally construed to conform with this principle.

Louisville Trust Co. v. *Glenn*, 66 F. Supp. 872;
Madison Mercantile Products v. *Frank Ix & Sons*, 7 F. R. D. 615.

Barron and Holtzoff speaking of Rule 13, state:

"The purpose and effect of the rule . . . is to permit any claim that defendant has against the

> plaintiff to be asserted as a counterclaim, thereby avoiding circuity of action. It is immaterial whether the counterclaim is legal or equitable or in contract or in tort, or even whether it has any connection with the plaintiff's claim. . . ." Barron and Holtzoff "Federal Practice and Procedure", Vol. 1, § 391.

There appears to be no valid reason, either as a matter of comity or public policy, for any limitation whatsoever on the type of counterclaim that may be pleaded against a sovereign. As Mr. Justice Story said in *The Santissima Trinidad and The St. Ander* (7 Wheat. 283, 353, 354):

> ". . . It may therefore be justly laid down as a general proposition, that all persons and property within the territorial jurisdiction of a sovereign, are amenable to the jurisdiction to himself or his courts; and that the exceptions to this rule are such only as by common usage and public policy, have been allowed, in order to preserve the peace and harmony of nations, and to regulate their intercourse in a manner best suited to their dignity and rights. It would, indeed, be strange if a license implied by law from the general practice of nations, for the purposes of peace, should be construed as a license to do wrong to the nation itself, and justify the breach of all those obligations which good faith and friendship, by the same implication, impose upon those who seek an asylum in our ports. . . ."

II

Assuming that counterclaims against a sovereign should be limited to those arising out of the transaction or subject matter of the suit, the counterclaims here asserted are within that limitation.

The basis of pronouncements by some of the lower courts to the effect that a counterclaim can be asserted against a sovereign only if it arises out of the subject matter of the action, or the same transaction, seems to have been mainly a misunderstanding of some of the decisions of this Court, particularly those involving admiralty law. This limitation may also have had its origin in outmoded principles of pleading. The test that has been used by such courts to determine what type of counterclaim may be asserted against a sovereign appears to be the same as that incorporated in the Federal Rules of Civil Procedure, under Rule 13(a) entitled "Compulsory Counterclaims", rather than the broader conception of permissive counterclaims.

Although, as we have heretofore pointed out, there is no good reason and no controlling authority for so limiting counterclaims against a sovereign, it is the petitioner's contention that the counterclaims asserted by it in this action were the kind of counterclaims described in Rule 13(a) and did arise out of the same subject matter or transaction upon which the plaintiff's cause of action is based.

In *Moore* v. *New York Cotton Exchange*, 270 U. S. 593, 610, the court construed Equity Rule 30, the forerunner of present Rule 13, as follows:

> ". . . 'Transaction' is a word of flexible meaning. It may comprehend a series of many occurrences,

depending not so much upon the immediateness of their connection as upon their logical relationship . . . [T]he facts relied upon by the plaintiff rarely, if ever, are, in all particulars, the same as those constituting the defendant's counterclaim. . . ."

This broad interpretation of the word "transaction" was applied in the *United States* v. *National City Bank of New York* (83 F. 2d 236, 239), which involved facts essentially similar to those here under consideration.

See also

Lesnik v. *Public Industrial Corp.*, 144 F. 2d 968, 975.

In *Rosenthal* v. *Fowler* (D. C. N. Y. 1952), 12 F. R. D. 388, the court cites with approval Professor Moore as follows:

". . . Professor Moore, in 3 Moore's Federal Practice (2d ed.) Par. 13.13 wisely suggests:

"'An all-embracing definition [of 13(a)] cannot be given, nor is one desirable. The same flexibility and same empirical treatment is necessary in connection with "transaction or occurrence" that has been advocated and discussed in connection with "cause of action". [2 Moore's Federal Practice (2d ed.) Par. 2.06.] * * * [C]ourts should give the phrase "transaction or occurrence that is the subject matter" of the suit a broad realistic interpretation in the interest of avoiding a multiplicity of suits. Subject to the exceptions, [not instantly relevant] any claim that is logically related to another claim that is being sued on is properly the basis for a compulsory counterclaim; only claims that are unrelated or are related, but within the exceptions, need not be pleaded.'"

Here, The Republic of China and the City Bank have been conducting banking business with each other for many

years. When this action was commenced, the monetary balance of all these years of transactions was in favor of the City Bank. It would appear entirely improper and inequitable to separate a single incident—(the Shanghai-Nanking Railway deposit account) from this long series of occurrences so as to grant a recovery to The Republic of China. It would be a narrow and forced construction of Rule 13(a) to ignore the many years of prior banking relationships in favor of one isolated circumstance. Therefore, these counterclaims should be allowed to stand because they are part of a chain of events, logically connected, one link of which makes up the subject matter of the suit brought by The Republic of China.

III

Sovereign immunity as defined by the lower courts does not conform to the present state of the law or with the ideals of responsible government.

The doctrine of sovereign immunity, as it has been applied in this case, permits a foreign government to be financially irresponsible. It places the American courts in the position where they must ratify unconscionable repudiation of debts freely assumed by foreign governments with American institutions. It is such a result as here achieved that has brought the concept of sovereign immunity into such great disfavor. This doctrine from various angles, and none the least from the ethical standpoint, has been criticized from bench[1] and bar[2] for many years.

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[1] See *Chisholm* v. *Georgia*, 2 Dall. 419, 471, 1 L. Ed. 440; *United States* v. *Wilder*, 3 Sumn. 308, 315-317, Fed. Cas. No. 16,694; *Wallace* v. *United States*, 142 F. 2d 240, 243.

[2] See *"Historical Approach to the Doctrine of Sovereign Immunity"* 13 La. L. Rev. 476; *Borchard "Governmental Responsibility in Tort"* 34 Yale L. J. (1924), 129, 229, 36 Yale L. J. (1926), 757, 1039.

Judge Frank, in the opinion below, criticized the doctrine (R. 68, *ante*, p. 6).

In *United States* v. *Lee* (106 U. S. 196), Mr. Justice Miller said (p. 206):

> ". . . As no person in this government exercises supreme executive power, or performs the public duties of a sovereign, it is difficult to see on what solid foundation of principle the exemption from liability to suit rests . . ."

and again on pages 208, 209:

> "Under our system the *people*, who are there [in Britain] called *subjects*, are the sovereign. Their rights, whether collective or individual, are not bound to give way to a sentiment of loyalty to the person of a monarch. The citizen here knows no person, however near to those in power, or however powerful himself, to whom he need yield the rights which the law secures to him when it is well administered. When he, in one of the courts of competent jurisdiction, has established his right to property, there is no reason why deference to any person, natural or artificial, not even the United States, should prevent him from using the means which the law gives him for the protection and enforcement of that right."

In 1946, Mr. Justice Frankfurter, dissenting in *Kennecott Copper Corp* v. *State Tax Commissioner* (327 U. S. 573, 580-581) said:

> "Even while the Civil War was raging Lincoln deemed it important to ask Congress to authorize the Court of Claims to render judgments against the Government. He did so on the score of public morality. 'It is,' wrote Lincoln in his First Annual Message, 'as much the duty of Government to render prompt justice against itself in favor of citizens as

it is to administer the same between private individuals. The investigation and adjudication of claims in their nature belong to the judicial department.' 7 Richardson, Messages and Papers of the Presidents, 3245, 3252. Both the United States and the States are immune from suit unless they agree to be sued. Though this immunity from suit without consent is embodied in the Constitution, it is an *anachronistic survival of monarchical privilege, and runs counter to democratic notions of the moral responsibility of the State.*

"Not so long ago this Court acted on the realization that 'the present climate of opinion . . . has brought governmental immunity from suit into disfavor.' *Keifer & Keifer* v. *R. F. C.*, 306 U. S. 381, 391. Today the Court treats governmental immunity from suit as though it were a principle of justice which must be safeguarded even to the point of giving a State's authorization to be sued the most strained construction, whereby a federal court sitting in Utah is made to appear not a 'court of competent jurisdiction.' Thus, while during the last seventy-five years governmental immunity from suit, as *a doctrine without moral validity*, has been progressively contracted, the Court now takes a backward step by enhancing a discredited doctrine through artificial construction." (Emphasis added)

Why should not a government be held liable for its just debts as any other person? It has been said that we must recognize the "dignity" of a sovereign,[1] but is it

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[1] *The Schooner Exchange*, 7 Cranch 116.

In *The Roseric* (254 Fed. 154, 158), the court, in construing *The Exchange* case, said:

"The immunity there accorded was not due to a lack of judicial power. The power was assumed, but its exercise was waived out of a due regard for the dignity and independence of a sister sovereignty, with whom this nation was at peace. The implication is that to insist upon jurisdiction in such in-

really undignified to pay one's debts? If a responsible sovereign government has so little regard for its dignity that it has flatly refused to pay its just obligations, it does not seem likely that its dignity could suffer any further humiliation by having those debts recognized in a court of law. In truth, upon close examination, there appears to be no sound reason why our courts should countenance such a doctrine.

The doctrine of sovereign immunity has never been adequately explained. In *United States* v. *Lee* (*supra*), the court said, at p. 207:

> "And while the exemption of the United States and of the several States from being subjected as defendants to ordinary actions in the courts has since that time [*Cohens* v. *Virginia,* 19 U. S. 264 (1821)] been repeatedly asserted here, the principle has never been discussed or the reasons for it given, but it has always been treated as an established doctrine. . . ."

In *United States* v. *Shaw* (309 U. S. 495, 501), the court attributed the doctrine to several vague origins, saying:

> ". . . The reasons for this immunity are imbedded in our legal philosophy. They partake somewhat of dignity and decorum, somewhat of practical administration, somewhat of the political desirability of an impregnable legal citadel where government as distinct from its functionaries may operate undisturbed by the demands of litigants. . . ."

It should be noted that very early in our history our government enacted legislation[1] which authorized counter-

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stances likely would be considered by the foreign sovereign as a reflection upon its dignity and an interference with its independence, and would tend to strain and possibly disrupt amicable relationships."

[1] Act of March 3, 1797, Sess. II, Chap. XX.

claims to the extent of the government's claim where the government voluntarily sued. This statute has been liberally construed and, although no mention is made in the statute of the scope of a counterclaim to be allowed against a sovereign, this Court, in *United States* v. *Wilkins* (6 Wheat. 135, 144, 145), expressly stated that such counterclaims may arise out of transactions not the subject matter of the suit. In construing the third and fourth sections of the statute the Court said:

> ". . . The terms of these sections are very broad and comprehensive . . . There being no limitation as to the nature and origin of the claim for a credit which may be set up in the suit, we think it a reasonable construction of the act, that it intended to allow the defendant the full benefit at the trial of any credit, *whether arising out of the particular transaction for which he was sued, or out of any distinct and independent transaction,* which would constitute a legal or equitable set-off, in whole or in part, of the debt sued for by the United States. The object of the act seems to be to liquidate and adjust all accounts between the parties, and to require a judgment for such sum only as the defendant in equity and justice should be proved to owe to the United States. If this be the true construction of the act, which we do not doubt, the defendant might well claim a credit in this suit for the sums due to him, *even if they had grown out of distinct and independent transactions,* for he is legally, as well as equitably, entitled to them. . . ." (Emphasis added)

If "dignity" of the sovereign is a basis for the granting of immunity, is there any reason why our courts should recognize a dignity in a foreign sovereign which they have not seen fit to recognize in the United States Government? Certainly the fact that here the foreign sovereign has refused to pay its debts to a corporation organ-

ized under the laws of the United States ought to make the answer to this question apparent.

But, assuming that there may still be valid reasons for granting friendly foreign sovereigns a limited immunity from suit in our courts, the immunity should not include a protection from counterclaims such as are asserted here.

In the *Gloria* (286 Fed. 188), the court said (p. 194):

> "There is no principle of public law exempting a sovereign state from its obligations under the law. It should not be assumed that a state desires to deny or evade its obligations. There may be sound reasons of public policy why a state should be immune from the harassment of litigation in forums and under conditions not agreeable to the state. But, once the state has chosen its forum, there seems little reason in law or policy why it should not be subject to the substantive requirements of law and justice."

In *People* v. *Brandreth* (36 N. Y. 191, 196, 197), Judge Hunt, dissenting from a majority opinion which dodged the issue of sovereign immunity, said:

> "Although a State cannot be sued, I think it is subject to a set-off, like individuals, when it comes into court as a plaintiff, and this, both upon principle and authority. When it becomes a suitor, it waives, for the time, its dignity as a sovereign. It lays aside its strong arm, by which it can at once enforce its own claims, and submits itself to the arbitration of the courts, and to its practice and its proceedings. For this purpose, it is like an individual or an inferior corporation, and becoming voluntarily a party to a suit, no good reason can be given why it should not be bound by the same rules that are applicable to other parties in the same position. . . ."

When a foreign sovereign comes into our courts it waives its immunity and should be prepared to meet defenses and counterclaims just as any other litigant. A foreign sovereign which voluntarily institutes a contest in our courts has no right to expect that our courts will condone an unfair contest by depriving the defendant of the weapons with which to defend himself.

IV

The indebtedness of The Republic of China is payable at the petitioner bank.

In the courts below the petitioner contended, as one of the grounds for sustaining the counterclaims, that they were payable at the City Bank and that, therefore, under decided cases and pursuant to § 147 of the Negotiable Instruments Law of the State of New York, they should be considered as a direction to pay the obligee to the extent of the bank account sought to be recovered in the action.

> *United States* v. *National City Bank of New York*, 83 F. 2d 236, 239.

The petitioner does not deem it necessary to devote any extended argument to this contention, because it believes that sufficient grounds have been presented in this brief as to why the counterclaims should be allowed. However, in the opinion of the Court of Appeals, reference was made to this argument and the second counterclaim was dismissed for the reason that the Treasury Notes therein referred to, although payable at the Shanghai Branch of the City Bank, were not payable at the City Bank, because a foreign branch of a national bank association must be treated as a separate entity under

§ 25 of the Federal Reserve Act; 12 U. S. C. §§ 601-604 (R. 69-70).

It would be unfortunate if such an interpretation of § 25 of the Federal Reserve Act should be permitted to remain on the books as authoritative. The language of that section is:

> "Every national bank association operating foreign branches shall conduct the accounts of each foreign branch independently of the accounts of other foreign branches established by it and of its home office, and shall at the end of each fiscal period transfer to its general ledger the profit or loss accrued at each branch as a separate item."

It is true that, with respect to certain banking transactions, foreign and even domestic branches of a national bank have been treated by the courts as banking entities separate from each other and from the head office.

> *Pan American Bank & Trust Co.* v. *National City Bank*, 6 F. (2d) 762, 767;
> *In re Harris*, 27 F. Supp. 480;
> *Marlboro Trust Co.* v. *Elliott*, 86 F. (2d) 315, 316-17;
> *Bluebird Undergarment Corp.* v. *Gomez*, 139 Misc. (N. Y.) 742.

However, no matter how many branches, foreign or domestic, a national bank may have, it is still a single corporation. The bank as such is responsible for all its obligations, whether originating at the head office or at a branch. If a branch is closed, the bank at its head office must make good to all depositors and other creditors of the branch.

> *Sokoloff* v. *National City Bank of New York*, 130 Misc. 66, aff'd 223 App. Div. 754, aff'd 250 N. Y. 69;

Wallace v. *State Bank*, 7 Ark. 61;
Michie on "Banks and Banking", Vol. 1, Chap. 2, § 27;
Zollman on "Banks and Banking", §§ 1295 and 1296.

It has never before been suggested that a national bank cannot collect obligations owing to or payable at one of its branches, particularly when that branch has been closed, as is the case with the Shanghai Branch of the City Bank. Obviously a private individual or corporation could not collect a deposit account at the head office of a national bank, if he or it were in default in the repayment of a loan for a larger amount negotiated at one of the bank's branches. There can be no question that, in such a situation, the bank would be entitled to apply the balance in the deposit account to the payment of the loan, whether on the theory of a "banker's lien" or set-off.

There is no reason why the same rule should not apply to the deposit account of a foreign government or an agency of such government.

The finding by the court that the Notes mentioned in the first counterclaim, a direct obligation of the plaintiff herein held by one bank for the benefit of all others bound together in a syndicate to loan money to the plaintiff, was not "payable" at the bank here because by its terms it was payable at another bank of that syndicate (R. 69), represents a glorification of literalness and a denial of principle for which there can scarcely be found a precedent since the time of the rise of the courts of equity to prevent injustice by the too literal application of technicalities. The note was payable at one of the member banks of the syndicate and was held by Morgan & Co., the manager of the syndicate, for the benefit of all the members. The defendant here had a large participating interest (R. 24). Clearly, in principle, the note was "payable at the defendant", if that be a significant condition to its right to plead it as a counterclaim.

V

The plaintiff sovereign has no immunity from jurisdiction of American courts.

The District Court held that the defendant's counterclaims (set-off) were each the equivalent of an independent suit and in this pronouncement, the Court of Appeals concurred, saying:

> ". . . For the assertion against a sovereign government of a counterclaim or set-off, unrelated to the claim asserted by the sovereign in its suit, is the equivalent of an independent suit against that sovereign brought without its consent. . . ." (R. 68).

This coupled with the further statement of that same court that

> ". . . a friendly, foreign sovereign, recognized by the United States, cannot be sued in the courts of this country without its consent. . . ." (R. 67)

were the premises of a syllogism. The logical deduction from the major and minor premises above quoted creates the situation by which the foreign sovereign is permitted to determine that the defendant bank may not plead certain facts which would defeat the sovereign's claim.

The Court of Appeals was not unmindful of, or indifferent to, the peculiar result thus achieved by the plaintiff sovereign's motion to exclude the counterclaims and observed that the doctrine of sovereign immunity was one considered basically immoral by many. But in maintaining this position, the court expressed itself as bound by the premises which it accepted. It was in this expression of helplessness to do complete justice here that the court erred, and its error was two-fold.

These two errors are: first, that the court considered these counterclaims independent suits, which they are not; and, second, that as independent suits, the court had no jurisdiction over the plaintiff as to the counterclaims.

The petitioner, in Points I, II and III hereof, has shown that there is no basis for the first limitation assumed by the District Court and the Court of Appeals which excluded the present counterclaims as a proper pleading by the defendant to defeat the plaintiff's claim as against it.

We then come to the supporting statement, which is really the major premise of the two, that a foreign sovereign may not be sued without its consent. For this we may consider the position of the plaintiff sovereign as though the counterclaims were indeed independent suits.

Two questions are involved in an independent suit against a sovereign. One is—does the court have jurisdiction? The other, after the first has been affirmatively answered, is—what is the breadth of immunity which should be granted to a sovereign?

The United States Has Jurisdiction over the Plaintiff Sovereign

Since the United States is itself an independent sovereign and therefore supreme within its own territory, it has exclusive and absolute jurisdiction within that territory. This complete and universal jurisdiction is subject only to such limitations as the United States itself consents to place upon it. What limitations should be placed upon it becomes, therefore, a matter of national policy. These are the principles as to jurisdiction laid down by Chief Justice Marshall in the case of *Schooner Exchange* v. *M'Faddon* (*supra*, p. 14), who said:

". . . The world being composed of distinct sov-

> ereignties, possessing equal rights and equal independence, whose mutual benefit is promoted by intercourse with each other, and by an interchange of those good offices which humanity dictates and its wants require, all sovereigns have consented to a relaxation in practice, in cases under certain peculiar circumstances, of that absolute and complete jurisdiction within their respective territories which sovereignty confers."

This principal remains as true today as when enunciated in 1812.

In the present case, the foreign sovereign has voluntarily entered our courts and has asked our courts to exercise jurisdiction in a controversy between it and the defendant. By voluntary appearance here, the sovereign has requested this controversy presented by it to be settled in accordance with the laws of the forum. After defendant served its pleadings, putting in issue other factors in the relations between it and defendant, the sovereign asked the court to protect it against the legal result of these counterclaims. The sovereign says the United States courts have no jurisdiction to consider the effect of any dealings with defendant bank, other than those the sovereign itself presents.

John Marshall more than one hundred and forty years ago found that any granting of immunity was to be determined on practical international considerations. It is right and proper therefore to follow Marshall's thesis and practice in arriving at a conclusion here. The first question to be asked and answered is the one Marshall himself propounded—What are the "usages and received obligations of the civilized world"?

From this naturally arises the particular question as to what attitude the United States itself has now adopted

toward the problem of sovereign immunity and what immunity or lack thereof would be granted or withheld in the interest of the United States. In considering, then, what is the proper relation of our courts to this particular foreign sovereign suing to collect a bank account and the defendant to whom that sovereign owes far more than it is seeking to collect, we must consider the breadth of immunity which should be granted in such case under three headings:

(1) What precedents exist in the state of the law throughout the world at this time? Do other countries recognize such sovereign immunity? That question is one of international law.

(2) What is the attitude of the United States in its foreign relations towards the problem of sovereign immunity?

(3) What law should now be imposed in the interest of the United States in its world position and in accord with the principles of international law?

Democratic Countries Throughout Europe Do Not Now Generally Grant Immunity to Foreign Sovereigns Against Enforcement of Contracts Made Under Their Jurisdiction by Such Foreign Sovereigns

John Marshall wrote his famous opinion in the case of *Schooner Exchange* early in the nineteenth century. He found no precedents to guide him and he trod, as he said, "an unbeaten path". For the next fifty years the courts of all European countries, when faced with similar cases, abstained from exercise of jurisdiction over sovereign states. In general, European courts granted sovereigns immunity from all acts which commercially affected nationals of their own countries.

The situation is far different today. In this, the middle of the twentieth century, we observe throughout the

democratic countries of Europe almost universal remission of the classical doctrine of absolute immunity. Sovereigns are now held liable for the contracts which they make with citizens and corporations subject to the jurisdiction of a foreign country. Courts have even gone so far as to exercise initial jurisdiction over a sovereign by calling it to court and have ended with seizing sovereign property to satisfy the judgments. The practical difficulties of acquiring initial jurisdiction and of entering an affirmative judgment against the sovereign are not present in this case.

A few instances of this change which began in the last century may be mentioned by way of illustration.*

Belgium

Among the first which repudiated the doctrine of absolute immunity appears to be Belgium. In 1879, for the first time, an appellate court, the Court of Appeals of Ghent, restricted the immunity of a foreign state, where that sovereign state had acted commercially within Belgium. This case involved the purchase and sale of guano. The Court made a differentiation by granting immunity for governmental acts and exercising jurisdiction with respect to non-governmental acts.[1]

A little later, in 1888, the Civil Tribunal of Brussels made the same differentiation in a suit brought against the Minister of War of Bulgaria to secure payment on a contract with a Belgian company for the purchase of bullets for the Bulgarian Army. Here in spite of an express

* Citations to foreign cases are collected in the order in which reference is made to them in this text in Appendix B. The numbers in the text refer to the corresponding numbers in said appendix. When a case is quoted or paraphrased, the quotation referred to is given in the language used by the court. A literal English translation of each quotation is also given.

agreement in the contract between Bulgaria and the private merchant of Belgium that, for the settlement of any disputes arising under the contract, recourse must be had to Bulgarian courts, the Belgian court held that Bulgaria had acted as a private person in making this contract, thus submitting itself to all the civil consequences.[2]

That the purchased supplies were for the army is not considered. In 1903, the Court of Cassation had opportunity to decide on this question and it acknowledged the practice followed by some of the lower courts.[3] It therewith fixed the Belgian doctrine of no immunity for a government acting commercially.

Italy

The same progression of thought and judicial determination has occurred in Italy. As early as 1886, that is before the centralization of the judicial system, some of the regional courts of cassation were faced with this problem and decided to exercise jurisdiction over the foreign sovereigns when they had acted *iure gestionis*, as "*ente civile*" and not as "*ente politico*". The form of the act, not its purpose, was held decisive.[4] In 1892 the Court of Cassation of Venice exercised jurisdiction and condemned Austria to pay an Italian enterpriser who had done construction work on fortifications on the Austrian border of Venice before the separation of this Italian province from Austria.[5] After the centralization the highest Italian Court, the Court of Cassation, had first opportunity to decide on this point in 1925 [6] and it confirmed this decision a year later, when it judicially ascertained the indebtedness of the Roumanian government to an Italian merchant, who had sold to said sovereign a quantity of leather for army boots.[7] In 1935 this doctrine was again affirmed in a case involving commercial representation by the U. S. S. R. and it has been the accepted doctrine since that time.[8]

France

It appears that France hesitated much longer to accept the new doctrine of restricted immunity. In 1929 the Court of Cassation first exercised its jurisdiction, when a foreign sovereign had acted commercially within its jurisdiction.[9] This new doctrine became definitely fixed in 1936, when the Court of Cassation abruptly rejected an appeal from the Parisian Court. In so rejecting the appeal the high court stated that the introduction into and sale within France by a commercial representative of the U. S. S. R. of counterfeited samples of the memoirs of a poet constituted a tort committed through commercial acts for which the Government was liable.[10]

Switzerland

Switzerland followed the example of Belgium and Italy rather early. In 1918 in a case based upon a financial operation similar to the one in question today, the Swiss Supreme Court exercised its jurisdiction and ordered Austria to pay to Swiss nationals, bonds which the Austrian Imperial Royal Government had issued in 1914 as tax free and with 4½% interest and which had become due to be paid in Switzerland according to a clause in the indenture. This clause said that the payment of interest and the repayment of the capital would be made "with the Imperial Royal Treasury in Vienna in kronen or at places to be made known . . . in Switzerland for the pieces stamped in Switzerland in Swiss francs". The court grounded its decision on a finding that the legal relationship which was created between Austria and the buyers of the bonds belonged in the realm of private law, and that the whole transaction had taken place in Switzerland.[11] The facts in the case before the court today are essentially the same.

Austria

In 1950 Austria[12] definitely abandoned the doctrine of absolute immunity. This affirmance of the exercise of restricted jurisdiction, meaning liability for commercial acts, was evidenced by entry in the Book of Decisions (Spruchrepetitorium) of these principles.[13] Such an act means that the Supreme Court itself cannot overrule a principle therein laid down except by a certain majority of judges. In this opinion, the court, before coming to a decision, made a thorough analysis of the authorities on which it relied to show how it came to its conclusions. The court there first referred to the ways in which the problem of sovereign immunity had been dealt with in the courts of Austria up until that time as well as in Italy, Belgium, Switzerland, Egypt, Germany, England, United States, Czechoslovakia, Poland, France, Greece, Brazil and Chile. After considering these authorities, it then explored the arguments of writers learned in the law, particularly Austrian writers. It then considered international treaties existing in this general field and finally concluded that there was no acknowledged rule of international law according to which the so-called *acta gestionis* of a foreign state should be exempt from jurisdiction. The court then declared that there was no rule of the forum either to impose restrictions farther reaching than those of international law and that, therefore, no reason existed why a foreign state for *acta gestionis* should not be treated in its courts as a foreign private person would be treated. This, it concluded, would not violate international law, because any act which was recognized by international law as an act *iure imperii* would be respected by the Austrian domestic law as such.

For discussion of this case see American Journal of International Law, 1951, Vol. 45, p. 354.

Germany

With regard to Germany, it was only after World War II that some of its courts departed from the classical doctrine of absolute immunity expressly following the example of other countries. Before this change the highest German court had reached a conclusion strikingly similar to the lower court in this case.[14] In 1951, however, the Court of Appeals in Hamm allowed a restitution action of the former (Jewish) owner of real property sold to the Italian state during the Nazi regime, as the Italian state in this transaction had appeared as the subject of private rights and obligations.[15] In 1953, the Landgericht in Berlin as well did not grant immunity for the bombed-out ruin of the Latvian Legation in Berlin against plaintiff, who had sold such real property in 1939 because of racial persecution.[16] Again in 1953, the Landgericht in Kiel had adjudicated compensation for damages which had arisen out of an accident on a Danish bus which belonged to the Danish State Railway.[17] The Court made the same differentiation of the state as a sovereign and as a subject of private law, because sovereigns more and more participate in economic activities and because their creditors would be damaged, if not given appropriate legal protection.

In regard to Great Britain the State Department in a letter discussed *post* (p. 43, and reproduced for the convenience of the court in its entirety, Appendix C) has stated:

> ". . . There are evidences that British authorities are aware of its (the doctrine) deficiencies and ready for a change. . . ."

There appears to be ample precedent that the divine right of kings is not now an accredited doctrine in the democratic states of Europe.

Attitude Expressed by the State Department for the United States, in Its Foreign Relations

The State Department has expressed most clearly the position of the United States in regard to the right of a foreign country in our courts in respect to immunity. In a letter by the then Acting Legal Adviser, dated May 19, 1952, addressed to the Acting Attorney General, Philip B. Perlman, it says:

> "The Department of State has for some time had under consideration the question whether the practice of the Government in granting immunity from suit to foreign governments made parties defendant in the courts of the United States without their consent should not be changed. The Department has now reached the conclusion that such immunity should no longer be granted in certain cases. . . ."
>
> See *supra*, p. 42. Text of Letter, Appendix C, *post*, p. xvii.

The State Department indicates that the attitude of the United States towards sovereigns suing in United States courts has changed over the years and that this change has been in more recent times a rapid one. The two theories of sovereign immunity are set forth with the clearest possible indication that the State Department favors the "restrictive", not the "absolute" theory of sovereign immunity.

In so stating the policy, the writer of the letter, speaking for the State Department, points out that most of our allies adhered to, or are tending towards this restrictive theory and only those of the different philosophy as to private property have continued the full acceptance of the absolute theory.

The State Department is then careful to point out that this, which it terms a shift of policy by the executive branch, cannot control the courts, but, as the granting of sovereign immunity to a foreign litigant is to a large extent a matter of proper relations within the family of nations (thus adopting the Marshall thesis), this shift of policy is clearly the reason why the courts should reconsider the position of a friendly sovereign as a litigant.

Much has been said and written as to whether or not it was within competence of the State Department to publish such a letter and if this would be "controlling" on the courts. The petitioner believes that it is not necessary to enter into any controversy concerning the limits of the three independent branches of our Government or specifically, if a pronouncement of our State Department would be "controlling" on the courts.

The petitioner wishes to rely upon the letter from the State Department only to this extent; that this Department, charged with maintaining friendly relations between nations and of recognizing the existence of unfriendly relations, when such unhappily arise, has, in the course of its obligations, observed a shift of policy in other countries relating to the question before this Court—the breadth of sovereign immunity—and has called this to the attention of the law enforcement department of this Government. The petitioner conceives this letter from the State Department as in the nature of testimony by an expert witness in respect of foreign relations.

The State Department has begun, also, to exemplify its views here by the type of treaties of friendship and commerce which it is making with other countries. These waive the immunity under a standard formula as follows:

"No enterprise of either party, including corporations,

associations, and government agencies and instrumentalities, which is publicly owned or controlled, shall, if it engages in commercial, manufacturing, processing, shipping or other business activities within the territorities of the other Party, claim or enjoy, either for itself or for its property, immunity therein from taxation, suit, execution of judgment or other liability to which privately owned and controlled enterprises are subject therein."

Treaties containing this or similar clauses have been concluded or are being negotiated with:

Denmark, Senate Exec. I. 82d Cong. 2d Sess. Art. 18(3) 1952;
Greece, Senate Exec. J. 82d Cong. 2d Sess. Art. 14(5) 1952;
Colombia, 1951 Art. 18(2);
Israel, Oct. 18, 1951, Exec. R. 82d Cong. 2d Sess.;
Uruguay, Nov. 23, 1949, Senate Exec. D. 81st Cong. 2d Sess.;
Ireland, Jan. 21, 1950, Art. 15, Treaties and Other International Acts Series, No. 2155;
Italy, Feb. 2, 1948, Art. 24, par. 6, Treaties and Other International Acts Series, No. 1965.

Reference should also be made to the case of *U. S.* v. *Deutsche Kalisyndikat Gesellschaft*, 31 F. (2d) 199, 201:

"The treaty existing between Germany and the U. S., like Art. 281 of the Treaty of Versailles, provides that, if the German Government engages in international trade, it shall not in respect thereof have or be deemed to have any rights, privileges or immunities of sovereignty."

The treaties above mentioned are consistent with another new provision which may be found in treaties being

negotiated by the United States. This is directed to the assurance that the nationals of the United States whose property is "nationalized" in other countries will be compensated. Such treaty provisions are inconsistent with the theory of absolute sovereign immunity. A typical provision of such a treaty reads as follows:

> "Property of nationals and companies of either Party shall not be taken within the territories of the other Party except for public benefit, nor shall it be taken without the prompt payment of just compensation. Such compensation shall be in an effectively realizable form and shall represent the full equivalent of the property taken; and adequate provision shall have been made at or prior to the time of taking for the determination and payment thereof."[1]

The Acts of The Republic of China Set Forth in the Counterclaims Are Acts of a Private Law Nature

The first counterclaim relates to an obligation evidenced by a note of The Republic of China to pay dollars in the United States. This note by The Republic of China was pledged by the Pacific Development Company to a syndicate of banks, including the defendant, and ultimately became the direct obligation of The Republic of China to pay to that said syndicate a large sum of money. Over $300,000 of this, not including interest thereon, is now due to the City Bank.

As to the second counterclaim, the sovereign received directly from the City Bank funds on notes of the sovereign payable at the branch of the City Bank in Shanghai where the funds were made available to the plaintiff sov-

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[1] Treaty of the United States with the Kingdom of Greece, Article VII (3), signed on behalf of the parties August 3, 1951, ratified by the United States Senate on July 21, 1953.

ereign. The sovereign here too became voluntarily indebted to the defendant, an American institution, on a contract freely entered into. It may, however, in regard to the obligations of this second counterclaim, be of some significance to consider the balance of the obligations here reflected as of the close of the year 1948, the last year in which any payments were made on its obligations to the City Bank. During that year, the Bank, as shown in the second counterclaim, advanced to the plaintiff about $137,790.60. Within that same year, the sovereign paid to the Bank on principal of loans previously made, the sum of $89,759 with accrued interest then outstanding on its obligations. This left a total amount unpaid of $390,033.60. In that same year, 1948, the plaintiff transferred through the Shanghai branch of the City Bank $200,000 to the City Bank's head office in New York, for the creation of a deposit account in the name of the Shanghai-Nanking Railway Administration. It is this deposit which the plaintiff sovereign now seeks to collect.

The commercial nature of the dealings of the plaintiff with the defendant as set forth in each of the counterclaims is clear.

Decisions of foreign courts cited *supra*, pp. 38-42 have been on states of fact so analogous to the operations of the defendant here that one may consider them in point of law identical. Contracts made with an American entity; money made voluntarily payable in dollars in the United States, are in themselves sufficient criteria to bring this financing into the category of acts of a private law nature.

What Law Should Now Be Imposed in the Interest of the United States

It is respectfully suggested that if the principles laid down by the lower court ever had any validity, they

were the expressions of the law which existed as of yesterday. As shown above they appear to be narrower than the principles laid down by Mr. Justice Marshall in his great decision of 1812, for there he found that only in three great classes of cases should the sovereign have unlimited immunity. These were the person of the sovereign, the sovereign's ambassador and troops (other warlike appurtenances) of a foreign prince. This was in 1812. One hundred and forty years have changed the circumstances and with it a concept of the functions of government. With this must come a narrower application of sovereign immunity.

Economic thinking is no longer *laissez-faire*. The United States no longer is dependent upon foreign capital for its development (although foreign investment is still welcome). It has itself become the greatest lending country in the world and both from our Government and from persons, corporate or otherwise within the United States, friendly foreign governments have borrowed for their ever expanding functions of government; their economic development.

The United States today stands with vast potential powers as to other countries, but with no hegemony over the territory of any other.

This position of the United States must be considered. It is at the present time the greatest creditor nation in the world. It is endeavoring through the realm of economics to assist all nations to economic freedom and a high standard of living. To this end, American institutions are urged to loan and to invest in foreign countries. New capital equipment creates the surplus out of which may arise a higher standard of living. The question before this Court is—are these loans investments under normal commercial rules or is the borrower to be considered as

financially irresponsible, even though capable of enforcing its obligations in the courts of the United States?

The United States is in a position to determine by its leadership and example the degree of responsibility which should be assumed by sovereigns, voluntarily if they will, imposed upon them if necessary, in their borrowings and other business dealings within the United States.

The nexus between a decision in this case and the problems of nationalization of private property in foreign countries and many other problems yet to arise under the Point IV and other investment programs, is obvious.

If it is assumed that from the standpoint of precedent the lower court had some justification for its decision, it seems the conclusion is inevitable that it applied the law of a bygone era. But it did not consider that its pronouncement was the last word on the subject, for it definitely said that if there was any marked diminution of that "hoary doctrine"—this theory of absolute sovereignty—it must look to Congress or the Supreme Court.

Congress has never legislated on this subject, nor is there any reason for it to do so. The pattern as to the treatment of foreign sovereigns is considered and a precedent established not only for this country but for other countries as well by an early decision of this Court. By tradition, therefore, as well as by inherent power, this Court has the authority and the duty to determine this matter. It is for this Court to pronounce the law of today.

CONCLUSION

The City Bank should be allowed to assert its counterclaims against The Republic of China so that the bank account held by the City Bank in the name of the Shanghai-Nanking Railway Administration may be used by the City Bank as a reduction and partial payment of the debt owed it by The Republic of China, and the judgment of the court below should be reversed.

Respectfully submitted,

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August 31, 1954.

APPENDIX A

Section 25 (b) of the Federal Reserve Act, 12 U. S. C. Section 632, first paragraph.

"Notwithstanding any other provision of law, all suits of a civil nature at common law or in equity to which any corporation organized under the laws of the United States shall be a party, arising out of transactions involving international or foreign banking, or banking in a dependency or insular possession of the United States, or out of other international or foreign financial operations, either directly or through the agency, ownership, or control of branches or local institutions in dependencies or insular possessions of the United States or in foreign countries, shall be deemed to arise under the laws of the United States, and the district courts of the United States shall have original jurisdiction of all such suits; and any defendant in any such suit may, at any time before the trial thereof, remove such suits from a State court into the district court of the United States for the proper district by following the procedure for the removal of causes otherwise provided by law. Such removal shall not cause undue delay in the trial of such case and a case so removed shall have a place on the calendar of the United States court to which it is removed relative to that which it held on the State court from which it was removed."

Section 25 of the Federal Reserve Act, 12 U. S. C. Section 604.

"Every national banking association operating foreign branches shall conduct the accounts of each foreign branch independently of the accounts of other foreign branches established by it and of its home office, and shall at the end of each fiscal period transfer to its general ledger the profit or loss accrued at each branch as a separate item.

Dec. 23, 1913, c. 6, § 25, 38 Stat. 273; Sept. 7, 1916, c. 461, 39 Stat. 755."

Section 147 of the New York Negotiable Instruments Law.

"Where the instrument is made payable at a bank it is equivalent to an order to the bank to pay the same for the account of the principal debtor thereon."

Rule 13(a) of the Federal Rules of Civil Procedure.

"(a) *Compulsory Counterclaims.* A pleading shall state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party's claim and does not require for its adjudication the presence of third parties of whom the court cannot acquire jurisdiction, except that such a claim need not be so stated if at the time the action was commenced the claim was the subject of another pending action. As amended Dec. 27, 1946, effective March 19, 1948."

"(b) *Permissive Counterclaims.* A pleading may state as a counterclaim any claim against an opposing party not arising out of the transaction or occurrence that is the subject matter of the opposing party's claim."

APPENDIX B*

Foreign Court Decisions

1. *Rau* v. *Duruty*, Court of Appeals of Ghent, March 14, 1879, Journal de Droit international privé 1881 p. 82.

> ". . . Ce principe (souveraineté des nations) peut valoir lorsqu'un gouvernement, restant dans les *limites de sa mission gouvernementale*, prend des mesures dans l'intérêt de sa conservation ou pour des actes que lui dicte l'intérêt général, mais il ne peut plus en être question alors que le gouvernement vend du guano, et . . . passe des actes et des contrats qui, de tout temps et partout, ont été considérés comme des *contrats commerciaux* soumis a la juridiction des tribunaux de commerce . . ." Translation, *post*, p. xi.

2. *Re Minister of War of Bulgaria*, Civil Tribunal of Brussels, Dec. 29, 1888, Pasicrisie, 1889-3-62, Pandectes Périodiques, 1889, No. 309.

3. *Re Liège-Limburg Railway*, Court of Cassation, June 11, 1903, Pasicrisie, 1903-1-294. By annulling the decision of the Court of Appeals of Brussels denying jurisdiction it declared that such court had wrongly applied art. 92 of the Constitution,—stating that litigation concerning civil rights and political rights of the citizens belonged to the exclusive competence of the courts,—and

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* Reports of cases decided by courts of continental countries of Europe are not usually given under the names of parties thereto as customary in American reporting. However, the cases below cited, have been further identified by reference to one or more of the principal parties involved. Italics, when appearing in the texts of the cases cited, have been added. Translations following are numbered to correspond to texts translated.

it gave such article a new interpretation, reversing its own decision of 1842, the Court reasoned:

> ". . . Att. que la règle du droit des gens qui proclame l'indépendance des nations découle du principe de leur souveraineté n'est pas en cause; — Att. que la *souveraineté n'est engagée que par les actes de la vie politique de l'Etat;*— Que les actes par lesquels la puissance publique s'affirme sont régis à l'intérieur par le droit constitutionnel et échappent, à raison de la séparation des pouvoirs, au contrôle de l'autorité judiciaire, que leurs effets en dehors du territoire ne relèvent que du droit international et sont soustraits, à ce titre, à l'appréciation des tribunaux tant du pays que de l'étranger;— Mais att. que l'Etat ne doit pas se confiner dans son rôle politique, *qu'en vue des besoins de la collectivité, il peut acquérir et posséder des biens, contracter, devenir créancier et débiteur; qu'il peut même faire le commerce, se réserver des monopoles ou la direction de services d'utilité générale;*— Que, *dans la gestion de ce domaine* ou de ces services, l'Etat ne met pas en oeuvre la puissance publique, mais fait ce que des particuliers peuvent faire et, partout, *n'agit que comme personne civile ou privée*— Que lorsqu'en cette qualité, il est engagé dans un différend, apres avoir *traité d'égal à égal* avec son co-contractant ou a encouru la responsabilité d'une faute étrangère à lordre politique, la contestation a pour objet un droit civil du ressort exclusif des tribunaux aux termes de l'art. 92 de la constitution;— Att. que les Etats étrangers sont, en tant que personnes civiles et au même titre que les autres étrangers, justiciables des tribunaux belges; . . . *que si l'Etat étranger peut saisir nos tribunaux de poursuites contre ses débiteurs, il doit répondre devant eux à ses créanciers.*" Translation, *post*, p. xi.

4. ***Typaldos, Council of Greece at Naples*** **v.** ***The Asylum of Aversa,*** Court of Cassation of Naples, March

27, 1886 Giurisprudenza Italiana, 1886 I. l. 228, the Greek council in official capacity had consented to pay for the maintenance of a Greek subject in an Italian asylum:

> "Attesoche cotesto sistema, che assume prestigio di autorità dalla giurisprudenza sinora proclivi il più delle volte a seguirlo procede da un equivoco originario, da cui derivano tutte le consequenze contrarie ai principii generali del diritto. Che fondamento di diritto internazionale sia la sovranità ed indipendenza degli Stati, ni uno potrebbe contestare; e che in consequenza di tale principio ogni stato nell'esercizio dei suoi potero sia sottratto alla giuridizione degli altre, egli e egualmente indubitato. Ma l'equivoco sta nel considerare lo stato unicamente et sempre come *ente politico*, dovechè non gli si puo negare l'attività ancora di *ente civile*, che opero nel senso di acquistare diritto e contrare obligazioni in rapporti privati, comi ogni altro ente fisico o morale capace dell'esercizio dei diritti civili. Conciossia chè importa certamente allo stato, che è a capo di gravissimi interessi di profittare di tutte le forme e rapporti contrattuali ondi si compie il movimento economico nei commerci della communanza civile considerata nel rapporto più generale dei popoli tra loro. Or il volere che anche cotesti rapporti contrattuali possero regolati dal diritto della gente, importa confondere cose ed idee diverso, e spingere un principio giusto alle piu assurdi conclusioni." Translation, *post*, p. xii.

5. ***Fisola*** **v.** ***Court of Cassation of Rome,*** **Oct. 12, 1893 Giurisprudenza Italiana, 1893 I. l. 1213.**

6. ***Commerciai Representative of U. S. S. R.*** **v.** ***Ditta Tesini e Malvezzi, Court of Cassation,*** **June 12, 1925, Corte di Cassazione, 1925, No. 1024, a contract for purchase and sale of silk cocoons.**

7. *Roumanian Government* v. *Trutta*, Court of Cassation, March 13, 1926, Corte di Cassazione, 1926, No. 1661; Giurisprudenza Italiana, 1926 I. 1. 774, Foro Italiano 1926-1-584.

"Scrittori e giudici hanno meditato su questi argomenti ed indicato la risposta. L'attuale nozione della sovranità dello Stato rifugge da quel concetto di assolutismo, che ispirava l'antica dottrina. . . . schivando l'opinione che nella communità delle nazioni la vera situazione degli Stati sia d'interdipendenza, bisogna riconoscere che in qualche modo tutte le sovranità sono l'un l'altra reciprocamente sottornesse. La sovranità dello stato puo ricevere senza, e non *ogni atto compiuto dallo stato ne interessa la sovranità.* Non si puo ammettere una esplicazione della sovranità intesa alla violazione di quei diritti maestatici, che sono reputati essenziali, tra cui à la giurisdizione sulle persone operanti nel territorio nazionale a sulle cose esistenti nel medesimo. Lo stato pur essendo sempre persona per eccellenza di diritto pubblico, alla capacità di diritto pubblico aggiunge, sia nella sfera del suo diritto interno, che nei rapporti esteriori di diritto internazionale, la capacità di diritto privato, la quale esso ha per il solo fatto della sua esistenza, confermato dal riconoscimento della sua persona giuridica internazionale non essendo concepibile un'associazione di nomini dotata di autonomia politico e di sovranità, la quale non abbia e non eserciti anche rispetto al diritto privato la facoltà di compiere atti con efficaccia giuridica e di valersi delle norme giuridiche. *Nell'esercizio della capacità di diritto privato, rimanendo integra la sua qualità di persona pubblica, lo stato non mette in opera la sua sovranità, ma agisce come un particolare a simiglianza di qualsiasi privato,* e dà origine a rapporti che in nessun modo si puo riuscire a confondere con quelli di diritto pubblico.

Se è necessario che quanto compire nella sfera elevata del potere pubblico vada esente dal giudizio dei tribunali di un altro stato, per impedire che si sovrappongano alla sua sovranità e le rechino offesa, non avviene altrettante per i suoi atti che non sono emanazione della sovranità, ma esplicazione della *natturale e commune attività umana, e possono in egual modo compiersi da qualsiasi individuo capace.* Da essi sorgono rapporti di diritti privato, a cui rimane estranea ogni idea di sovranità. E siffatta loro natura spontaneamente li *assogetta alla giurisdizione dei tribunali di un altro stato nei casi, in cui secondo le loro leggi, possono giudicare su stranieri.* D'altra parte questi tribunali, senza menomare la sovranità dello stato, a cui appartengono, non possono abdicare ad una giurisdizione, che sorge dall 'essenza del rapporto giuridico e dal modo in cui operano i soggetti che v'intervengono.

"E arbitrario supporre che per il solo fatto di conchiudere un contratto con uno stato straniero, il privato implicamente rinunci alla giurisdizione nazionale e si sottoponga a quelle dell'altro contraente." Translation, *post,* p. xii.

8. *Re Commercial Representative of U. S. S. R.,* Court of Cassation, Aug. 3, 1935, Giurisprudenza Italiana, 1935, I. l. 109.

"In tale sentenza, (Governo Rumeno v. Trutta, supra) infatti, fu nettamente precisato che lo Stato estero, in ordine agli *atti compiuti come soggetto di diritto patrimoniali, e che in quanto talinon ne mettono in causa la sovranità, non può invocare la immunità giurisdizionale* che gli é propria per tutti gli atti compiuti nell'esercizio delle sue funzioni sovrane. Lo Stato, per gli atti della prima specie, si mette nelle condizioni di un privato, assoggettandosi come questo anche eventualmente alla giurisdizione dei tribunali di altro Stato, nei casi in cui questi sareb-

bero competenti a giudicare rispetto a stranieri." Translation, *post*, p. xiv.

9. *U. S. S. R.* v. *Chaliapine*, Court of Cassation, Feb. 19, 1929, D. P. 1929 I 73, S 1930 I 49, copied in Niboyet, Les immunités de juridiction, en droit francais, des états étrangers, Révue Gén. Dr. Int. Publ. 1936, 525, 530. The Court of Cassation accepted jurisdiction based on the following consideration:

". . . Attendue que la saisie arrêt contestée a été pratiqué sur la représentation commerciale en France de l'U. S. S. R.; que l'arrêt constate que cette représentation commerciale manifeste son activité commerciale dans tous les domaines; que ces manifestations ne peuvent apparaître que comme des *actes de commerce auxquels le principe de la souveraineté des états demeure complétement étranger.*" Translation, *post*, p. xiv.

10. Court of Cassation, Dec. 15, 1936, 1937, Nouvelle Revue de Droit international privé 568.

11. *Finanzministerium* v. *Dreyfus*, Supreme Court of Switzerland, March 13, 1918, BGE 44 I 49, kk oesterreich.

"Hierbei ergibt sich, dass der fragliche Grundsatz" (der Exterritorialitaet des auslaendischen Staates gegenueber der inlaedischen Gerichtsbarkeit) "des Voelkerrechtes keineswegs als allgemein und vorbehaltlos anerkannt gelten kann. Wohl folgert eine weitverbreitete Lehre aus der voelkerrechtlich vorausgesetzten Souveraenitaet und gegenseitigen Unabhaengigkeit der Staaten, dass ein Staat nicht nur, soweit er in Ausuebung seiner Hoheitsgewalt (iure imperii) handelt, sondern der Regel nach auch, soweit er als Subjekt von Privatrechtsverhaeltnissen (iure gestionis) auftritt, keiner fremden Gerichtsbarkeit untersteht. Dieser Auffassung huldigen ins-

besondere die deutsche und die oesterreichische, sowie auch die franzoesische, englische und nordamerikanische Praxis (vgl. L. v. Praag, Juridiction et Droit international publique, p. 390ff, 400-405). Ihr steht jedoch schon seit 1886 die italienische und seit 1903 die belgische Praxis gegenueber, wonach ein fremder Staat in seiner Eigenschaft als Traeger privater Rechte allgemein gleich einer Privatperson vor dem inlaendischen Richter belangt werden kann (v. Praag, Juridiction et Droit international privé, p. 406, Niemeyers Zeitschrift fuer internationales Privat- und oeffentliches Recht XVI, 1906, p. 243). Und im gleichen Sinne treten den in ihren Laendern herrschenden Meinungen entgegen: France: André Weiss, Dr. int. pr. V. p. 96-115, Germany: Friedrich Stein, Zivilprozessordnung (10. Auflage des Grauppschen Kommentars) p. 16." (Reference to Hamburg Act. II § 1 ziff 5, Annuaire de l'institut XI, 437.) Translation, *post*, p. xv.

12. *Hoffmann* v. *Jiri Dralle*, Supreme Court of Austria.

Decision of May 10, 1950, 1 Ob 167/49 and 1 Ob 171/50, XXIII Entscheidungen des oesterreichischen Obersten Gerichtshofes in Zivil—und Justizverwaltungssachen 1950, p. 304 No. 143.

". . . Diese *Freigabe der acta gestionis an die Jurisdiktion der einzelnen Staaten* ist in der Entwicklung, die die wirtschaftliche Betaetigung der Staaten genommen hat, begruendet. Die klassiche Immunitaetslehre ist in einer Zeit entstanden, da eine jede wirtschaftliche Betaetigung eines Staates im Auslande mit seiner politischen zusammenhing, . . . Einen Unterschied zwischen privaten Rechtsgeschaeften und Souveraenitaetsakten zu machen, war daher nicht gerechtfertigt; ganz anders heute, da die Staaten sich selbt kommerziell betaetigen und mit In-und Auslaendern, wie der vorliegende Streitfall zeigt, im

Wettbewerb stehen. Die klassische Immunitaetslehre hat deshalb heute ihren Sinn verloren und kann daher auch ratione cessante nicht mehr als geltendes Voelkerrecht anerkannt werden." Translation, *post*, p. xv.

13. The rules are: (Spruchrepetitorium No. 28)

I. Auslaendische Staaten sind nach *Voelkerrecht* nur insoweit von der Gerichtsbarkeit der inlaendischen Gerichte eximiert, als es sich um Akte handelt, die sie in Ausuebung der ihnen zustehenden Hoheitsgewalt vorgenommen haben.

II. Auch nach *innerstaatlichem* Recht sind auslaendische Staaten in allen Rechtsstreitigkeiten aus Privatrechtsverhaeltnissen der inlaendischen Gerichtsbarkeit unterworfen. Translation, *post*, p. xvi.

14. In the decision reported RGZ 111, p. 375 (1905), the Supreme Court of Germany held in a case involving a collision that a counterclaim had to be stated on the same material facts as the claim.

15. *Re Italian Government*, Court of Appeals in Hamm, Germany, April 4, 1951, 2 Rechtsprechung zum Wiedergutmachungsrecht, 1951, p. 258.

16. *Re Latvian Legation*, Landgericht Berlin, October 3, 1953, 4 Rechtsprechung zum Wiedergutmachungsrecht, 1953, p. 368.

17. *Re Danish State Railway*, Landgericht in Kiel, Germany, March 19, 1953, Neue Juristische Wochenschrift, 1953, p. 1718.

TRANSLATIONS.

1. Court of Appeals of Ghent, March 14, 1879, Journal de Droit international prive, 1881, p. 82.

". . . This principle (sovereignty of nations) has its value when a government staying within the limits of its governmental mission takes measures which are in the interest of its conservation or which are dictated to it by the general interest, but that ceases to be the question when the government sells guano, and . . . passes acts and enters contracts which at all times and everywhere were considered commercial contracts . . ."

3. Court of Cassation, June 11, 1903.

". . . It is true that the law of nations proclaiming the independence of nations deriving from the principle of their sovereignty is not involved here;— It is true that the sovereignty is only involved through acts of the political life of the State;— It is true that the acts through which the public power affirms itself are governed domestically by the constitutional law and because of the reason of the separation of powers, they escape the control of the courts;— It is true that their results outside of the territory affect only the international law and they are, by this, susceptible only to the consideration of the country itself as well as of other countries;— But it is true that the State does not have to confine itself to its political role; that in view of the needs of the collectivity, it can acquire and possess goods, and enter contracts, it can become creditor and debtor; that it can also trade, can reserve to itself monopolies or the direction of services of general utility;— It is true that acting in this field or in these services, the State does not put in effect its public power, but it does that which

individuals can do, and, throughout, it acts just as a civil or private person;— It is true that when in this quality, it becomes engaged in a dispute, after having acted on the same footing with its contracting partner or it has taken the responsibility of a mistake, foreign to its political capacity, the conflict has for its object a civil right of the exclusive resort of the courts according to the terms of Art. 92 of the constitution;— It is true that the foreign States are, just as civil persons and in the same way as other foreigners under the jurisdiction of Belgian courts;— . . . It is true that if the foreign State comes into our courts to pursue its debtors, it should answer its creditors before these courts."

4. Court of Cassation, Naples, March 27, 1886.

"This system, acquiring authoritative ascendancy from the jurisprudence which is often prone to follow it, arises from an original ambiguity, from which originate all the consequences contrary to the general principles of law. No one can contest that sovereignty and independence of the States is the foundation of international law, nor can there be any doubt that as a consequence of such principle, each State, in the exercise of its powers, is beyond the jurisdiction of other States. But the ambiguity rests in considering the States solely and always as a political entity, since it cannot be denied to it to act as a civil entity, to operate in the sense of acquiring rights and assume obligations in private relationships, similar to a physical or artificial personality capable to exercise civil rights. Therefore the State, heading important interests, must take advantage of all contractual relationships to further the economic activity for commerce by the community of people, considered in their more general relationship. To subject these contractual relations also to the law binding on people means a confusion of different

things and ideas and the pushing of an equitable principle to the most absurd conclusions."

7. Court of Cassation, March 13, 1926.

"Writers and judges have pondered over these arguments and have given an answer. The present notion of State sovereignty recoils from the concept of absolutism furthered by the old doctrine. . . . avoiding the opinion that in the community of nations interdependence is the true status of the States, it becomes necessary to recognize that in some way all the sovereignties are linked reciprocally to each other. The sovereignty of the State exists by itself and not each act performed by a State affects its sovereignty. One cannot allow an explanation of sovereignty when it tends to violate those majestic rights which are reputed essential, among which belongs the jurisdiction over persons operating in the national territory and over choses existing in such territory. Although the State is always eminently a public law entity, in the sphere of internal law as well as in its external relationships of international law, it adds to such capacity that of the civil law, which devolves upon the State through the mere fact of its existence, confirmed by the acknowledgement of its international juridic personality, since it is inconceivable that an association of persons, endowed with political autonomy and sovereign, does not have and fails to exercise, even in relation to private law, those functions tending to the performance of acts having juridic efficacy and to avail itself of the juridic norms. The State, while acting under private law and without detracting from its capacity of public personality, does not employ its sovereignty, but acts as an individual like any other individual, and gives rise to relationships which in no way can be confused with those related to public law. While it is necessary that any action performed in the high sphere of public

domain be foreign to the jurisdiction of the Courts of another State, so as to prevent violations and offense to the sovereignty of the former, the same is not true for those acts which do not arise from sovereignty, but which are an exposition of the natural and common human activity, capable of being performed in a similar manner by any capable individual. Such acts give rise to private law relationships to which any idea of sovereignty is entirely extraneous. This, their nature, spontaneously submits them to the jurisdiction of the Courts of another State in those instances where, according to their laws, judgment may be passed upon aliens. On the other hand, these Courts cannot, without impairing the sovereignty of their State, waive a jurisdiction when it arises from the essence of the juridical relationship and from the manner of acting displayed by the parties appearing before it.

It is arbitrary to assume that an individual, by the mere fact of entering into a contract with a foreign state, implicitly waives national jurisdiction and submits to that of the other party."

8. Court of Cassation, Aug. 3, 1935.

"In this decision (*Roumanian Government* v. *Trutta, supra*) it was clearly established that the foreign State, in line with acts performed under the heading of private law and provided that such acts do not bring its sovereignty into play, cannot invoke jurisdictional immunity to which it is entitled for all acts performed in the exercise of its sovereign functions. The State, for the former acts, appears as a private individual, submitting as the latter even to the jurisdiction of the Courts of another State, where the Courts are competent to pass judgment upon aliens."

9. Court of Cassation, Feb. 19, 1929, D. P. 1929, I 73 S 1930 I 49.

". . . It is true that the contested attachment was served on the commercial representation (representative) of U. S. S. R. in France; that the decision finds that this commercial representation manifests its commercial activity in all fields; that these manifestations can only appear as commercial acts to which the principle of sovereignty of states is completely foreign."

11. Supreme Court of Switzerland, March 13, 1918, BGE 44 I 49 kk oesterreich. *Finanzministerium* v. *Dreyfus.*

"It hereby follows that the principle in question" (of the Extraterritoriality of a foreign state with regard to the domestic jurisdiction) "of the law of nations cannot be looked upon at all as general and without restriction. It is true that a widely recognized doctrine concludes from the sovereignty, presumed in the international law, and from the mutual independence of the states that a state not only in so far as it is acting in the exercise of its public power (*iure imperii*), but also then according to rule when or in so far it shows itself as a subject of relations of private law (*iure gestionis*), is not subject to any foreign jurisdiction. The same opinion is shown in the German and the Austrian as well as the French, the English and the North American practice (compare L. v. Praag, Jurisdiction et Droit international publique, p. 390ff, 400-405). Since 1886 a contrary view has appeared in Italian practice and since 1903 the Belgian practice, according to which a foreign state in its quality as holder of private rights can generally be brought before a domestic judge just as a private individual (v. Praag . . .). And in the same sense are opposed to the opinions

governing in their countries: France: Andre Weiss, Dr. . . ."

12. Supreme Court of Austria; Decision of May 10, 1950.

". . . This release of the *acta gestionis* to the jurisdiction of the different states is founded upon the development of the economic activity of the states. The classical doctrine of immunity originated in an era when every economic activity of a state in a foreign country was connected with its political activity, . . . there was no reason to make a differentiation between acts of a state of a private nature and of governmental; but this is very different today because the states themselves act commercially and compete with their own citizens as well as with foreigners, which is shown in the case at hand. Today the classical doctrine of sovereign immunity has therefore lost its sense and can no longer be recognized as international law presently in force."

13. The rules are (Spruchrepetitorium No. 28):

I. According to international law foreign states are immune from the exercise of jurisdiction of the domestic courts only in so far as acts are involved which they performed in the exercise of the sovereign power that belongs to them.

II. And according to the domestic law foreign states are subject to the domestic jurisdiction for all disputes arising out of relations of a private law nature.

APPENDIX C

Letter from Acting Legal Adviser Jack B. Tate, dated May 19, 1952, to Acting Attorney General Philip B. Perlman (XXVI, Department of State Bulletin, pp. 984-985 (June 23, 1952)).

My dear Mr. Attorney General:

The Department of State has for some time had under consideration the question whether the practice of the Government in granting immunity from suit to foreign governments made parties defendant in the courts of the United States without their consent should not be changed. The Department has now reached the conclusion that such immunity should no longer be granted in certain types of cases. In view of the obvious interest of your Department in this matter I should like to point out briefly some of the facts which influenced the Department's decision.

A study of the law of sovereign immunity reveals the existence of two conflicting concepts of sovereign immunity, each widely held and firmly established. According to the classical or absolute theory of sovereign immunity, a sovereign cannot, without his consent, be made a respondent in the courts of another sovereign. According to the newer or restrictive theory of sovereign immunity, the immunity of the sovereign is recognized with regard to sovereign or public acts (*jure imperii*) of a state, but not with respect to private acts (*jure gestionis*). There is agreement by proponents of both theories, supported by practice, that sovereign immunity should not be claimed or granted in actions with respect to real property (diplomatic and perhaps consular property excepted) or with respect to the disposition of the property of a deceased person even though a foreign sovereign is the beneficiary.

The classical or virtually absolute theory of sovereign

immunity has generally been followed by the courts of the United States, the British Commonwealth, Czechoslovakia, Estonia, and probably Poland.

The decisions of the courts of Brazil, Chile, China, Hungary, Japan, Luxembourg. Norway, and Portugal may be deemed to support the classical theory of immunity if one or at most two old decisions anterior to the development of the restrictive theory may be considered sufficient on which to base a conclusion.

The position of the Netherlands, Sweden, and Argentina is less clear since although immunity has been granted in recent cases coming before the courts of those countries, the facts were such that immunity would have been granted under either the absolute or restrictive theory. However, constant references by the courts of these three countries to the distinction between public and private acts of the state, even though the distinction was not involved in the result of the case, may indicate an intention to leave the way open for a possible application of the restrictive theory of immunity if and when the occasion presents itself.

A trend to the restrictive theory is already evident in the Netherlands where the lower courts have started to apply that theory following a Supreme Court decision to the effect that immunity would have been applicable in the case under consideration under either theory.

The German courts, after a period of hesitation at the end of the nineteenth century have held to the classical theory, but it should be noted that the refusal of the Supreme Court in 1921 to yield to pressure by the lower courts for the newer theory was based on the view that that theory had not yet developed sufficiently to justify a change. In view of the growth of the restrictive theory since that time the German courts might take a different view today.

The newer or restrictive theory of sovereign immunity has always been supported by the courts of Belgium and Italy. It was adopted in turn by the courts of Egypt and

of Switzerland. In addition, the courts of France, Austria, and Greece, which were traditionally supporters of the classical theory, reversed their position in the 20's to embrace the restrictive theory. Rumania, Peru, and possibly Denmark also appear to follow this theory.

Furthermore, it should be observed that in most of the countries still following the classical theory there is a school of influential writers favoring the restrictive theory and the views of writers, at least in civil law countries, are a major factor in the development of the law. Moreover, the leanings of the lower courts in civil law countries are more significant in shaping the law than they are in common law countries where the rule of precedent prevails and the trend in these lower courts is to the restrictive theory.

Of related interest to this question is the fact that ten of the thirteen countries which have been classified above as supporters of the classical theory have ratified the Brussels Convention of 1926 under which immunity for government owned merchant vessels is waived. In addition the United States, which is not a party to the Convention, some years ago announced and has since followed, a policy of not claiming immunity for its public owned or operated merchant vessels. Keeping in mind the importance played by cases involving public vessels in the field of sovereign immunity, it is thus noteworthy that these ten countries (Brazil, Chile, Estonia, Germany, Hungary, Netherlands, Norway, Poland, Portugal, Sweden) and the United States have already relinquished by treaty or in practice an important part of the immunity which they claim under the classical theory.

It is thus evident that with the possible exception of the United Kingdom little support has been found except on the part of the Soviet Union and its satellites for continued full acceptance of the absolute theory of sovereign immunity. There are evidences that British authorities are aware of its deficiencies and ready for a change. The reasons which obviously motivate state trading countries

in adhering to the theory with perhaps increasing rigidity are most persuasive that the United States should change its policy.

Furthermore, the granting of sovereign immunity to foreign governments in the courts of the United States is most inconsistent with the action of the Government of the United States in subjecting itself to suit in these same courts in both contract and tort and with its long established policy of not claiming immunity in foreign jurisdictions for its merchant vessels. Finally, the Department feels that the widespread and increasing practice on the part of governments of engaging in commercial activities makes necessary a practice which will enable persons doing business with them to have their rights determined in the courts. For these reasons it will hereafter be the Department's policy to follow the restrictive theory of sovereign immunity in the consideration of requests of foreign governments for a grant of sovereign immunity.

It is realized that a shift in policy by the executive cannot control the courts but it is felt that the courts are less likely to allow a plea of sovereign immunity where the executive has declined to do so. There have been indications that at least some Justices of the Supreme Court feel that in this matter courts should follow the branch of the Government charged with responsibility for the conduct of foreign relations.

In order that your Department, which is charged with representing the interests of the Government before the courts, may be adequately informed it will be the Department's practice to advise you of all requests by foreign governments for the grant of immunity from suit and of the Department's action thereon.

Sincerely yours,

For the Secretary of State:

JACK B. TATE
Acting Legal Adviser